A McKinsey Report

A Housing Agenda for New York City

PROPOSALS FOR CHANGE

Carter F. Bales and Anupam P. Puri

Preface

The past five years have seen dramatic changes in governmental policies and programs affecting housing in New York City. The list of new initiatives legislated during this period is impressive. In 1969, Rent Stabilization — a modified form of rent control — was imposed on the then uncontrolled housing stock. In 1970, the City Council enacted the first major revision of the rent control system since 1943, implementing the Maximum Base Rent program. In 1971, the State Legislature initiated the ultimate dismantling of all controls by enacting the Vacancy Decontrol law. Following this, three new housing institutions were created: the Housing Development Corporation in 1971, the Housing Court in 1972, and the Rehabilitation Mortgage Insurance Corporation in 1973. In addition, new subsidy programs were instituted and a number of existing programs strengthened.

It appears that 1974 will see further dramatic changes in City housing policy. The new City Administration has already announced its intention of dismantling the City's Housing & Development Administration, and of pressing for revisions to the rent control system. With the State Legislature now in session, Vacancy Decontrol and the MBR program have become the subjects of widespread debate. While pressures for repeal of these programs are mounting, thus far no coherent and workable substitutes have been proposed.

The purpose of this paper is to evaluate these various new programs as a basis for proposing modifications in housing policy and program emphasis. In it, we summarize and evaluate recent evidence on the City's housing situation and the impact of rent control revision, and then recommend some new departures for housing policy over the next few years. Since rent control is the most urgent preoccupation of policy makers, we devote considerable emphasis to the development of a proposed new system of rent regulation which we believe would provide a desirable alternative to both Vacancy Decontrol and the MBR program.

There is no attempt at originality — housing policy in the City does not need a new theory but a genuine and fair-minded attempt to absorb and understand the implications of facts that are already known. In this paper, we attempt to summarize and interpret these facts and make them available to those interested in the problem of housing.

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Introduction

The main purpose of this paper is to present some evidence on the impact of two recent revisions to the City's rent control program: the Maximum Base Rent program and the Vacancy Decontrol law. Sufficient data are now available on the results of these programs to enable informed judgments about whether they should be continued and, if not, what alternatives might appropriately be considered.

It is important, however, to view rent control as only one part of an overall City housing policy. In order to evaluate alternative systems of controlling or decontrolling rents, it is necessary to understand the housing problems to which the various housing programs are addressed, the impacts of these programs on housing quantity and quality, and the interrelationships among the various programs.

This paper is divided into three chapters. In Chapter 1, we summarize the trends in New York City's housing between 1950 and 1970, and identify the major problems confronting housing policy makers in the late sixties. Against this historical perspective, we review in Chapter 2 the rationale and structure of the new programs and program revisions which were introduced since 1970, emphasizing the Maximum Base Rent and Vacancy Decontrol programs. An evaluation of these programs suggests that a number of changes are needed both in the philosophy and content of housing policy in the City. Accordingly, in Chapter 3 we outline the principles which we believe should govern the City's housing policy over the next several years and present recommended changes in program structure and emphasis.

We have attempted to organize our discussion around three basic concepts which provide useful ways of summarizing and describing the City's housing problems: (1) the stock or quantity of housing; (2) the quality of services provided by the housing stock to tenants; and (3) the costs of these services. While these three concepts are interrelated - for example, a change in housing quantity will normally affect housing quality as well - it is important to differentiate them from each other.

Most people, when they think of housing, consider the housing stock as described by the total number of housing units available for occupancy.

The problem is thought of as being primarily a "shortage" of housing units, and the natural remedy is conceived of as "building more housing."

In fact, this approach to the housing problem is seriously incomplete and can lead to very distorted policy objectives. The size of the housing stock - as measured by the number of units - is an important but limited description of the housing situation. An increase in the number of units is necessary to house an increasing population, to provide for the new households that are formed each year, and to improve the choice of housing available to consumers. But for many reasons the quantity of housing is only loosely related to the quality of housing, and the latter is just as important a descriptor of the housing situation.

For example, in New York City, the size of the housing stock is growing rapidly enough to more than keep pace with population and household growth - the City does not have a "housing shortage" in the conventional sense. Despite this, the common perception that the City confronts a "housing crisis" of major dimensions is correct. What matters to most people is the kind and quality of services provided by the housing they occupy, and these have been declining in New York City at a dramatic pace, even while the stock of housing has been growing.

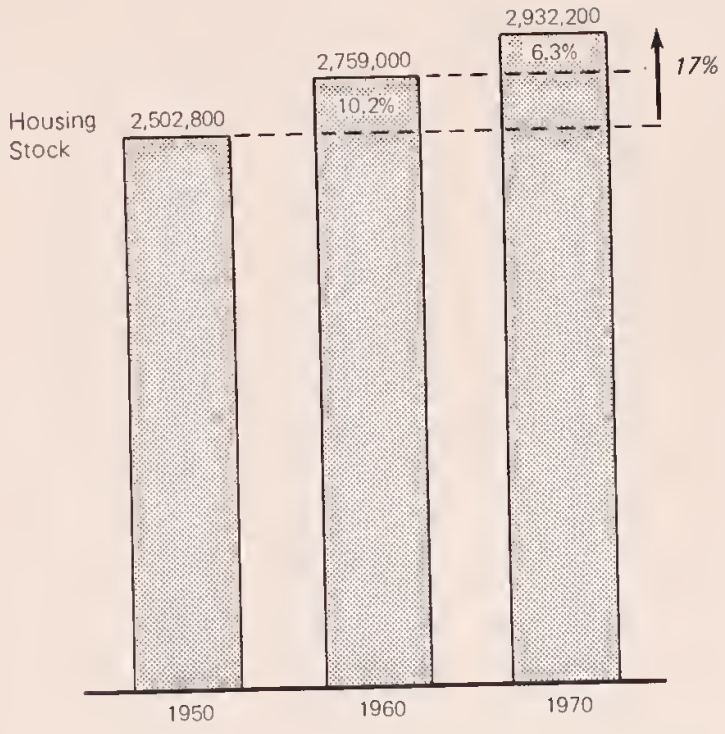
The quality of housing services - how well maintained the housing is, whether there are roaches or rats, whether essential services such as heat and hot water are provided - can decline substantially even with a static or growing number of housing units in total. An extreme example of this is the phenomenon of abandonment, in which the housing may continue to exist (and may be physically sound) but the housing services fall to zero because the owner abdicates his responsibility for providing them. It is the quality of housing services (as well as certain housing-related services, such as security and protection against crime) that is of primary importance to the majority of the City's households. And it is the unprecedented decline in these services, rather than a physical shortage of housing per se, that defines the unique nature of New York City's rental housing crisis.

Accordingly, we shall structure our discussion of the City's current housing problems around three basic concepts: the stock of housing, the quality of services provided by the housing stock, and the cost of providing these housing services. The cost of providing an acceptable level and quality of services is important for two reasons: (1) the cost of operating and maintaining housing, compared to rent levels, determines the quality of services that owners can and will voluntarily provide; and (2) the cost of providing an adequate level of housing services, compared to tenant incomes,

determines the budgetary burden on renters necessary to secure decent housing. Understanding the relationship between tenant incomes, ability to pay, actual rent levels, and the costs of providing housing services is thus key to understanding the rationale for the MBR and Vacancy Decontrol programs, assessing their impact, and evaluating whether they should be revised or replaced by other programs.

Exhibit I

New York City's housing stock increased 17 percent between 1950 and 1970 . . . .



New Construction	+ 323,000	+ 372,200
Conversions	+ 40,800	+ 26,000
Demolitions	– 107,600	– 110,000
Abandonments	– 0	– 195,000
Net	**+ 256,200**	**+ 173,200**

1-The Origins of the Housing Problem

The 20 years from 1950 to 1970 saw substantial improvement in the housing situation of most New York City residents. For most of this period, new construction levels were high, and the housing stock grew faster than the City's population. At the same time, the incomes of New York City residents outpaced the increase in rents. As a result, the per capita consumption of housing improved dramatically: the consumption of space increased substantially, the incidence of overcrowding declined, and the number of people living in substandard units fell.

Much of this improvement occurred between 1950 and 1965. During the second half of the 1960s, the housing situation took a dramatic turn for the worse. The gain in income for City residents slowed considerably; constraints on ability to pay adequate rents, together with a rigid and sometimes perverse system of rent control, led to a significant decline in the services afforded by the existing stock. Landlords, unable to maintain their properties at existing rent levels, either reduced the level of services or literally abandoned their buildings by the thousands. By 1970, the City was confronting a housing crisis of alarming proportions, which was, however, not a housing "shortage" in the conventional sense and could not be alleviated by the construction of more housing. Understanding the nature of this crisis is essential to understanding the rationale of the City's more recent housing programs and to evaluating their effectiveness.

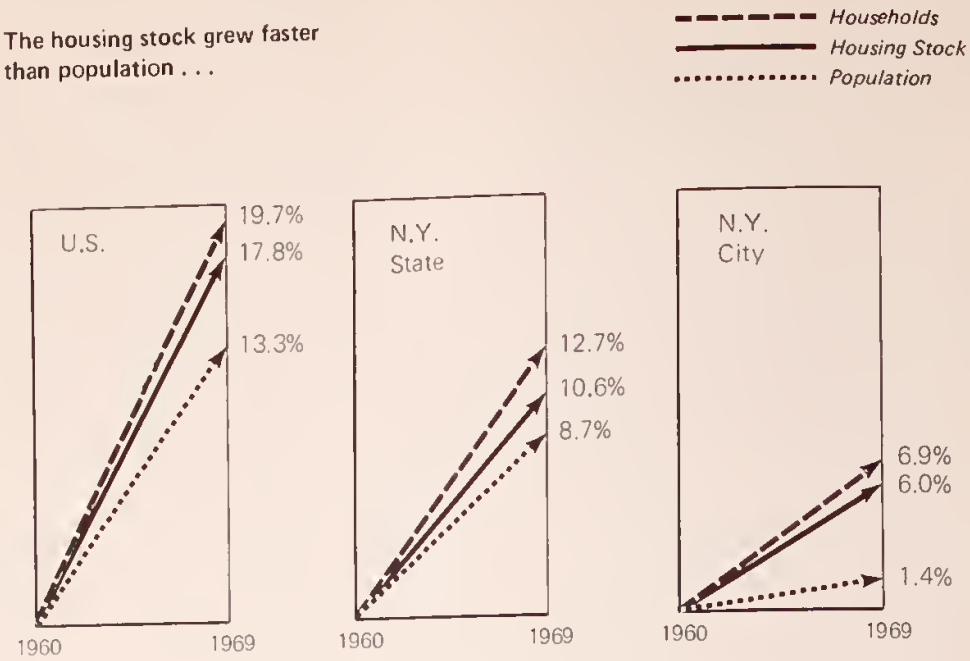
THE HOUSING STOCK

The size of the housing stock at any point in time is a product of four flows over the preceding period. New construction adds units to the existing stock of housing. Conversion of existing units may add units (when a large unit is split up into two smaller units) or may reduce the number of units (when small apartments are merged into fewer, larger units). Demolition, obviously, reduces the number of units; while abandonment results in the withdrawal of housing units from the active inventory available for occupancy, even though the housing may continue to stand until much later.

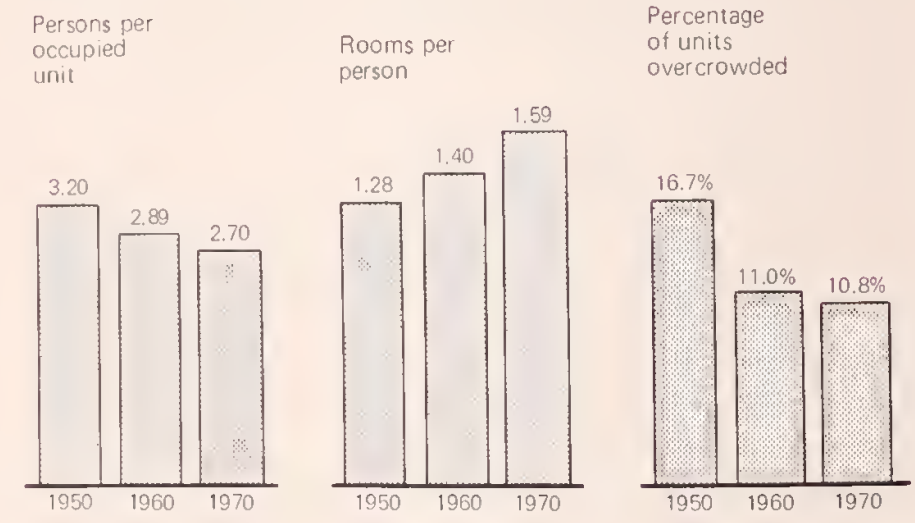
Exhibit I summarizes our estimates of the size of the City's housing stock in 1950, 1960 and 1970, and of the flows affecting the stock during

Exhibit II

The housing stock grew faster than population . . .



. . . Resulting in an improvement in the City's housing conditions . . . .



these two decades. Between 1950 and 1960, the stock grew by 250,000 units, for a total growth of about 10 percent. This rate of growth declined in the 1960s to about 6 percent over the decade.

Three general points should be emphasized about the City's housing stock:

Changes in the housing stock were very small, relative to the size of the existing stock. The average annual rate of new construction during the 1960s - 37,000 units - amounted to only 1.3 percent of the stock in 1960. Similarly, removals were typically less than 1 percent of the stock each year. Thus, most New Yorkers were little affected by either new housing construction or demolition of housing; of greater interest to the majority of households was the state of the existing inventory of housing.

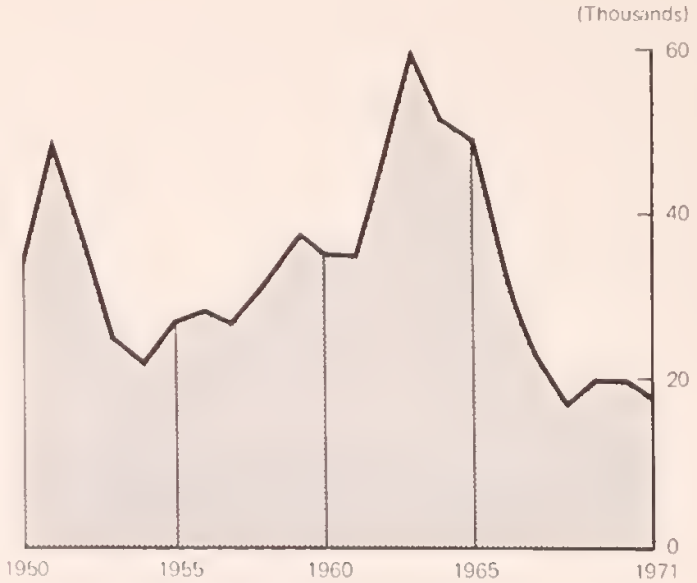
Even this slow growth of the housing stock was adequate to account for both population growth and household growth. Exhibit II shows that the increase in the number of housing units was larger than the increase in population, and also comfortably accommodated a substantial increase in the number of households in the City. While the growth in the City's housing stock was slower than that of the United States and of New York State, the City's population growth rate was, on a comparative basis, even lower. As a result, housing conditions in the City improved: Per capita consumption of space in the City rose substantially, the number of persons per housing unit declined, and the number of persons per room declined even faster. Thus, in terms of the availability of housing units and the amount of space per person, the housing situation in New York City improved over the past two decades.

The major difference between the 1950s and the 1960s was that the rate of removals from the housing stock (demolitions plus abandonments) jumped substantially in the latter decade. If this high rate of removals were to continue, new construction would bring about little additional growth in the overall housing stock. A doubling of the rate of new construction would add less than an additional 1 percent to the stock annually, especially since an increase in construction itself tends to increase the rate of removals. It is clear that a major emphasis on new construction will do little to solve the City's housing problem, without major efforts to reduce the abandonment of existing housing.

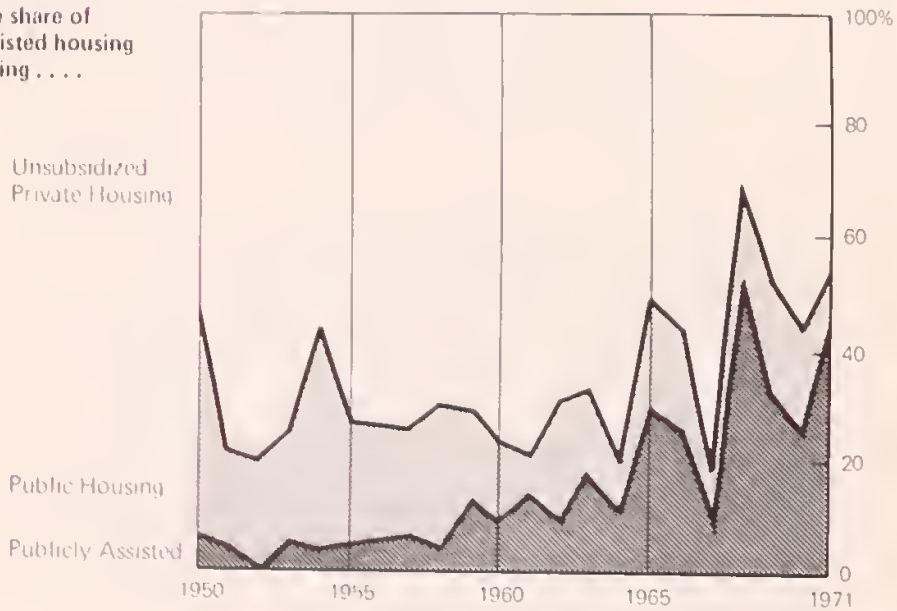
In order to provide a more complete description of what has been happening to the housing stock, we discuss in turn each of the four flows affecting the stock.

Exhibit III

New construction rates fluctuated dramatically . . .



. . . And the share of publicly assisted housing has been rising . . . .



New construction. Exhibit III shows the number of new construction completions for each year from 1950 to 1970, and the share of public housing and publicly assisted housing (the major components of this last category are the State and City Mitchell-Lama programs, together with several smaller interest rate subsidy and tax abatement programs). The exhibit demonstrates that:

- ¶ Total new construction has always been relatively low in the City. The rate has never risen above 60,000 units in 1 year, and even the relatively high rate sustained during the 1961-1965 period resulted from exceptional circumstances - especially the desire on the part of builders and developers to preempt a restrictive change in the zoning law that would substantially add to land acquisition and development costs.

- ¶ New construction rates were higher in the 1960s than in the 1950s. Over the decade as a whole, 50,000 more units were added in the 1960s than in the previous decade. Moreover, for the decade as a whole, the share of public and assisted housing programs rose only slowly, from 28.3 percent in the 1950s to 35.5 percent in the 1960s.

- ¶ However, a dramatic change has occurred since 1966. The rate of new construction fell almost continuously between 1966 and 1970, and the public sector provided 40 to 60 percent of the new housing constructed in each of these years.

Why were new construction rates in the City so low? The answer lies in a combination of high and rapidly increasing costs (which were nationwide trends, but were especially acute in New York City due to the high cost of acquiring land), a resulting high rent required to cover the debt service on the mortgage and maintain the housing, the inability to market new housing at these rents, and, finally, uncertainties with respect to the future of rent controls (especially the fear that controls would be extended to new housing).

Some of these factors are illustrated in Table 1, which shows the typical costs of a middle-income housing development in New York City. Typical rents for a two-bedroom apartment were $464 in 1970, an increase of over 100 percent in only 10 years. If renters were to spend 25 percent of their income on housing, this housing could be afforded only by people at income levels of $22,300 and up. And only 12 percent of the City's families have income levels that high.

Table 1

Costs and Rents for Middle-Income Housing*

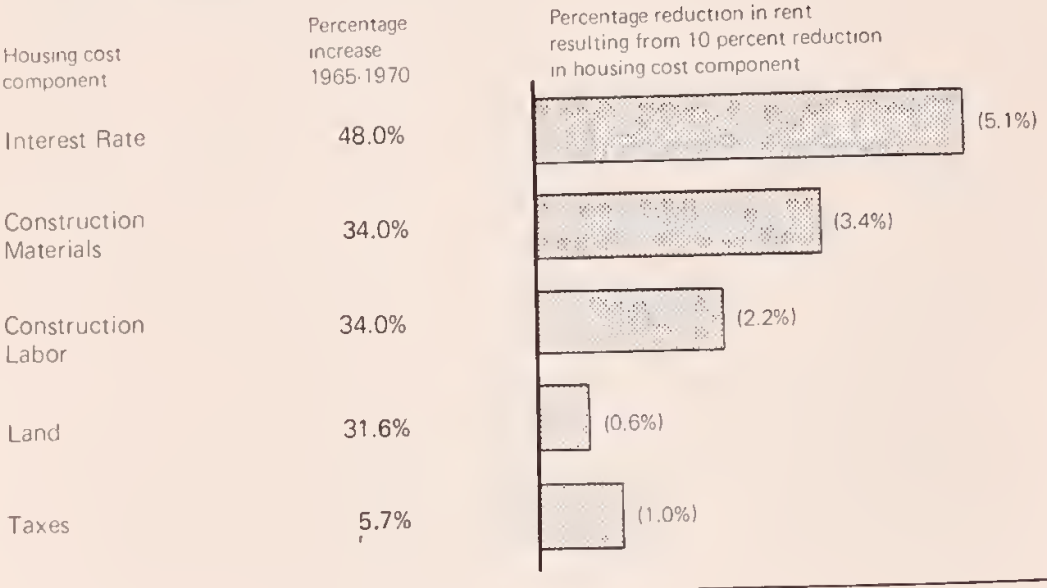
	1960	1970
Construction cost/unit	$17,000	$37,000
Nonconstruction cost/unit	4,000	8,000
Total project cost/unit	**$21,000**	**$45,000**
Median rent, two-bedroom apartment	$ 200	$ 464
Income level required	9,600	22,300
Percentage of households above this income level	29.0%	11.5%

* *City Mitchell-Lama housing projects.*

Exhibit IV shows how development and construction costs rose nationwide between 1965 and 1970. Costs in the City rose faster than the nationwide average. Particularly severe was the rise in interest rates on mortgage financing, which increased from levels of 5 to 6 percent in the mid-1960s to 8 to 9 percent toward the end of the decade.

Exhibit IV

Rents are most sensitive to changes in mortgage interest rate, which was the fastest rising component of housing cost . . . .



In order to mitigate these cost increases, a variety of Federal, State and City programs were developed. Exhibit V shows that most of these programs focused on reducing interest rates (since this is the largest cost element and has the highest impact on rent levels). In addition, the City provided assistance in condemnation of existing properties to make way for new buildings, in site acquisition and development, in abating or exempting property taxes on newly constructed housing, and in a variety of other ways.

Exhibit V

Most housing programs subsidize interest rates on long-term financing . . . .

Steps in the development process	Federal programs	State and City programs
1. Availability of developers/sponsors		
2. Site acquisition and zoning	Urban renewal	Land assembly and write-down Zoning incentives
3. Preconstruction activities	106 (b)	Seed money loans Technical assistance
4. Construction financing	312 115 221 (h)	Short-term loans
5. Construction		
6. Long-term financing	202 213 235 203 220 236 207 231 243	Interest rate subsidies Mortgage lending at below market rates
7. Rent-up and operation		

High and rising cost levels, together with limitations on Federal, State and City subsidy funds, have limited the effectiveness of public sector new construction programs in two ways. First, with higher costs, the number of units that could be financed directly or indirectly with public funds has diminished. Second, high costs imply high rentals, and therefore deeper subsidies per unit to make the housing available to households with low or middle incomes. With limited funds, these deeper subsidies can be provided to very few units; consequently, most of the housing built with City, State or Federal funds has benefited upper- and middle-income groups.

// During 1950 to 1970, we estimate that less than 21 percent of the new housing built directly benefited low-income groups.

Conversions. The rate of additions to the housing stock through conversions declined from the 1950s to the 1960s. This is likely to be a negligible source of new housing units in the future.

Demolitions. Demolitions occur primarily as a function of planned redevelopment of neighborhoods, inside or outside urban renewal areas. In addition, buildings are demolished by the City when they become health or safety hazards. Viewed over the past two decades, the number of demolitions has been relatively constant.

Abandonments. Abandonments of housing have become as important a factor in reducing the active housing inventory as demolitions, and are now embedded in the national consciousness as a unique and disturbing feature of the central city housing crisis. Three features of the abandonment problem are especially important:

- The rate of abandonment has climbed dramatically. During the 1950s, no recorded abandonment occurred. During the 1960s, about 10,000 units were abandoned annually. Moreover, this rate climbed from 4,000 to 6,000 units annually in the period 1960 to 1964 to an estimated annual rate of 18,000 to 20,000 abandonments at the end of the 1960s.

- Most of these abandoned buildings are still standing. Frank Kristof of the Urban Development Corporation has estimated that about 75 percent of the buildings abandoned in New York City are still standing. These buildings become major hazards to health and safety, encourage vandalism and crime, and can quickly blight an area with serious adverse effects on surrounding neighborhoods.

- Much of the housing abandoned in the City was structurally sound. While little is known about the details of abandoned buildings (because the abandonment is often not recorded until much later, by which time the building has been vacated and often vandalized beyond recognition), a disturbing phenomenon is that many of the abandoned buildings appear to be structurally sound. For example, the Citizens Budget Commission has estimated that 60 percent of the abandoned buildings could, with minor rehabilitation, have continued to provide decent housing to their occupants. Loss of

structurally sound housing through abandonment has come to be recognized as one of New York City's central housing problems.

Why do these abandonments occur? The basic reasons are by now well known: They include a process of neighborhood erosion caused by ethnic turnover, declining income, declining rents, and a significant reduction in landlords' ability to maintain their properties.

The overall stability of New York City's population masks a dramatic change in ethnic composition and income levels. Between 1950 and 1960, the proportion of nonwhites rose from 10 to 14 percent of the City's population; by 1970, this figure had increased to 21 percent. In addition, the newcomers were increasingly low-income families - between 1950 and 1960, the percentage of families earning less than $4,000 declined from 31.2 to 18.1 percent; by 1970, the percentage of families under $4,000 had grown to 32.9 percent. And this trend occurred despite a growth in the number of Social Security beneficiaries to over 1 million, with another 1.3 million persons on welfare.

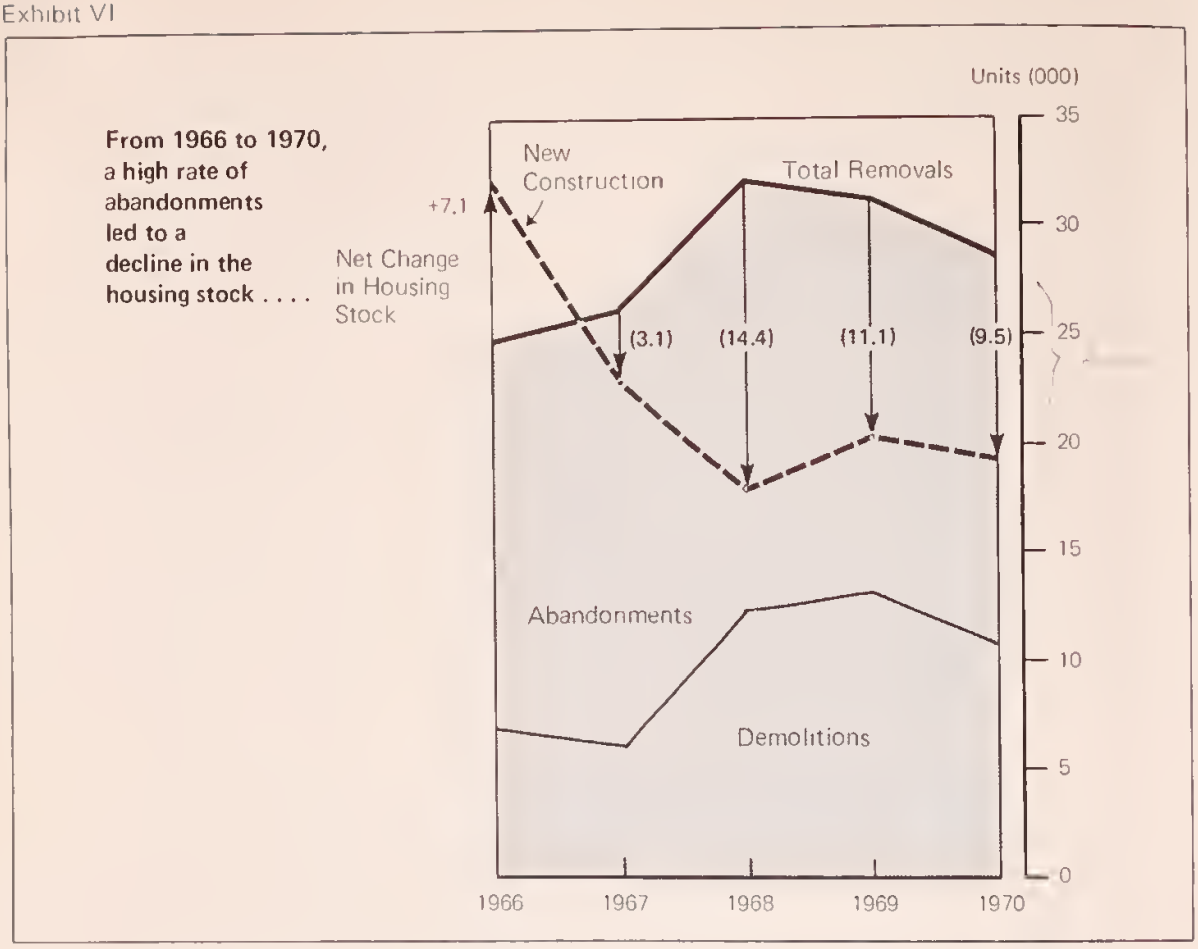
Given the low incomes of the new residents, previous rent levels in the City could not be sustained. Lower incomes, a relative concentration of the newcomers in limited areas of the City - with the existing neighborhood population fleeing, in part, due to racial prejudice - led to a process in which landlords significantly shortened their investment horizons, found their properties increasingly unsalable, decided to underinvest in maintaining those properties, and ultimately decided that it was more desirable to abandon their properties than to attempt to maintain them.

The process of abandonment had disastrous effects on housing in New York City. Not only were entire neighborhoods doomed, but the total stock of housing began to shrink (Exhibit VI). It became increasingly obvious that the prime focus of housing policy had to be to reduce the rate of abandonment and to ensure that the City's existing housing stock was preserved, rather than to raise the production rate of new housing.

SERVICES FROM THE HOUSING STOCK

The significant shift in the factors affecting the size of the housing stock during the late 1960s was much less important than the change in the quality of the existing housing stock, and in the nature of housing services afforded to its occupants.

Exhibit VI



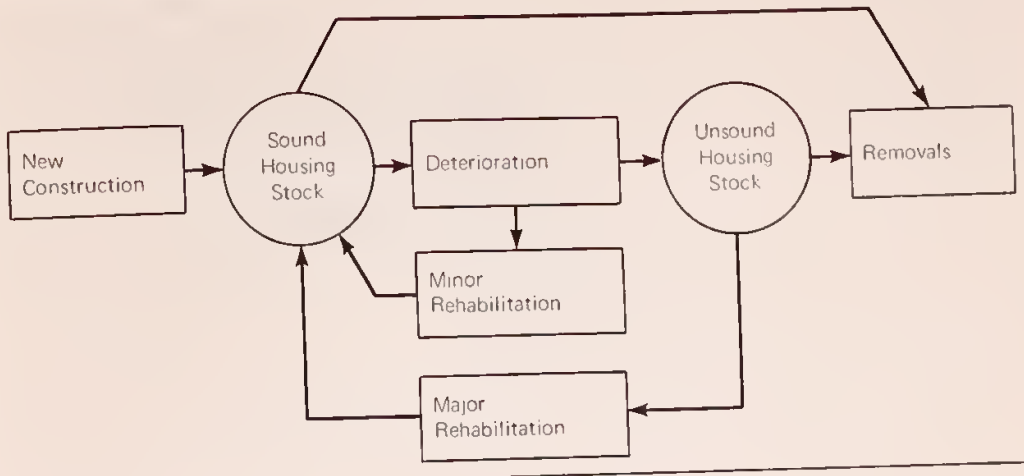
These changes can be measured in two ways - first, by the incidence of structural deterioration in the stock, and, second, by indicators describing the nature of housing-related services provided to tenants.

Structural Deterioration

Our simple framework of housing flows needs to be somewhat elaborated at this point (Exhibit VII). The existing housing stock can be divided into structurally sound housing and unsound housing. (Unsound housing in turn includes two categories - deteriorated housing, which is in a general state of disrepair, and dilapidated housing, in which major subsystems are not functioning or major structural defects exist.) New construction adds to the sound stock; but this sound stock deteriorates over time and becomes unsound. Minor rehabilitation can be used to arrest the process of deterioration, and return housing to a sound status; once dilapidated, major rehabilitation is required for this purpose. Removals occur from both the sound and unsound housing stock.

Exhibit VII

Flows in the housing stock



The major feature of New York City's housing crisis is a marked increase in the incidence of physical deterioration and dilapidation within the existing housing stock. While this contention is difficult to document precisely, a number of different studies have pointed to the same conclusions.

A study by the New York City-Rand Institute reported that over the period 1960 to 1967, the sound inventory grew by 2 percent, while the deteriorated inventory grew by 37 percent and the dilapidated inventory by 44 percent. Thus, in 1968, almost 20 percent of the City's housing stock was classified as unsound; in the rent controlled stock, this proportion was 29 percent.

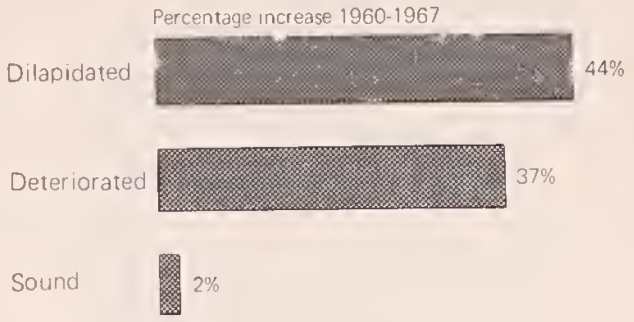
The 1970 census does not provide an estimate of housing deterioration; it does, however, confirm that the incidence of dilapidation increased from 161,000 to 177,000 units over the decade, thus raising dilapidated housing to 6 percent of the City's total housing stock.

Moreover, another study by the New York City-Rand Institute indicated that even among the sound stock, 39 percent of the units needed substantial repair amounting to over 20 percent of the building's rent roll. These repairs, if undertaken in 1968, would have cost over $2.1 billion.

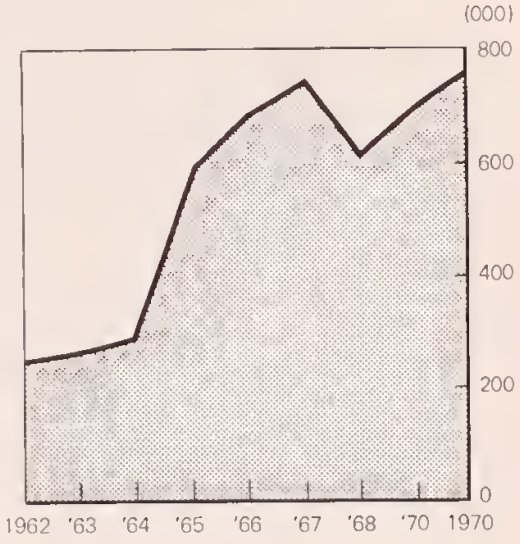
Another indication of structural deterioration is the incidence of housing code violations. While there are severe problems in interpreting these

Between 1960 and 1970, the quality of New York City's housing stock declined dramatically . . . .

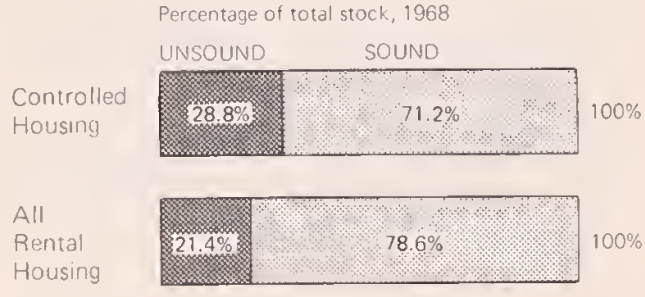
Between 1960 and 1967, the unsound stock grew faster than the sound stock . . . .



The number of pending code violations increased rapidly . . . .



By 1968, almost one-third of controlled housing was unsound . . . .



statistics, they show that the number of reported violations of the housing maintenance code that remained uncorrected grew from 240,000 in 1960 to 760,000 in 1969 (Exhibit VIII).

This marked deterioration in the quality of the existing housing stock grew out of a cost-price squeeze for landlords: the costs of operating housing, maintaining it adequately, and paying taxes and debt service rose much faster than rents. (This trend is discussed more fully in the next section.)

The City attempted to combat these problems through a number of programs. Overall, two major points are worth emphasizing: (1) none of these programs achieved a great deal, because they could not cope with the fundamental problem underlying housing deterioration, which was inadequate building revenue to sustain the housing stock; and (2) with these programs, the City became more and more involved in the operation and management of individual buildings, and in disputes between landlords and tenants. Market processes were increasingly ignored in favor of political processes that made the City Government a central party to all housing-related actions.

Major programs operated by the City to deal with structural deterioration included the following:

1. Code Enforcement. The Code Enforcement program was initially intended to provide for cyclical inspections of buildings, reporting of violations of the code, and enforcement of corrective action. Despite significant increases in both staff and funds, the program became an essentially reactive and passive program, with significant defects in program structure, operation and results. The shortcomings of the program included:

    - Weaknesses in the housing code itself (e.g., violations were not classified by seriousness).

    - Overload of the system. The system had become complaint-oriented (cyclical inspections fell to 2 percent of all inspections in 1969); weaknesses in the data base, and in the complaint intake and evaluation mechanism, resulted in serious program inefficiencies and much wasted effort. (Forty five percent of nonemergency inspections occurred with delays of 3 to 6 months.)

    - Ineffective sanctions. The offenders could be prosecuted only in the criminal court; delays in trying court cases were long (sometimes 18 to 24 months); and the typical fine in 1969 was $12 per case, or roughly $3 per violation. The inability to compel action by landlords made the program a grim joke.

Exhibit IX

Four levels of rehabilitation can be undertaken . . . .

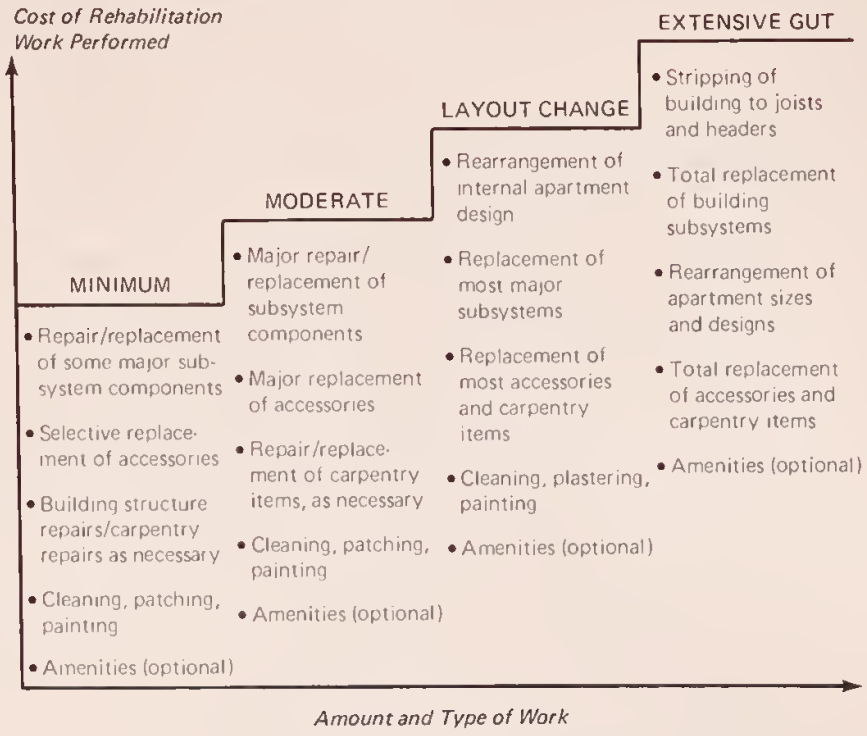


Exhibit X

Costs vary significantly by rehabilitation level . . . .

	Cost/unit, by level of rehabilitation			
Program	Minimum	Moderate	Layout	Gut
J 51	$1,100	–	–	–
OSI	$ 870	$ 3,700	–	–
312	$1,500	4,200	10,730	15,600
312	$2,000	5,600	–	–
Municipal Loan	–	$10,000	NA	17,600
221 (d) 3	–	–	$8,000 (estimated)	16,000-18,000

- Ineffectiveness of the punitive approach. For the low end of the housing stock, the basic problem was inadequate revenue; many owners lacked the financial means to remove code violations, and, if penalized, reacted by abandoning their buildings.

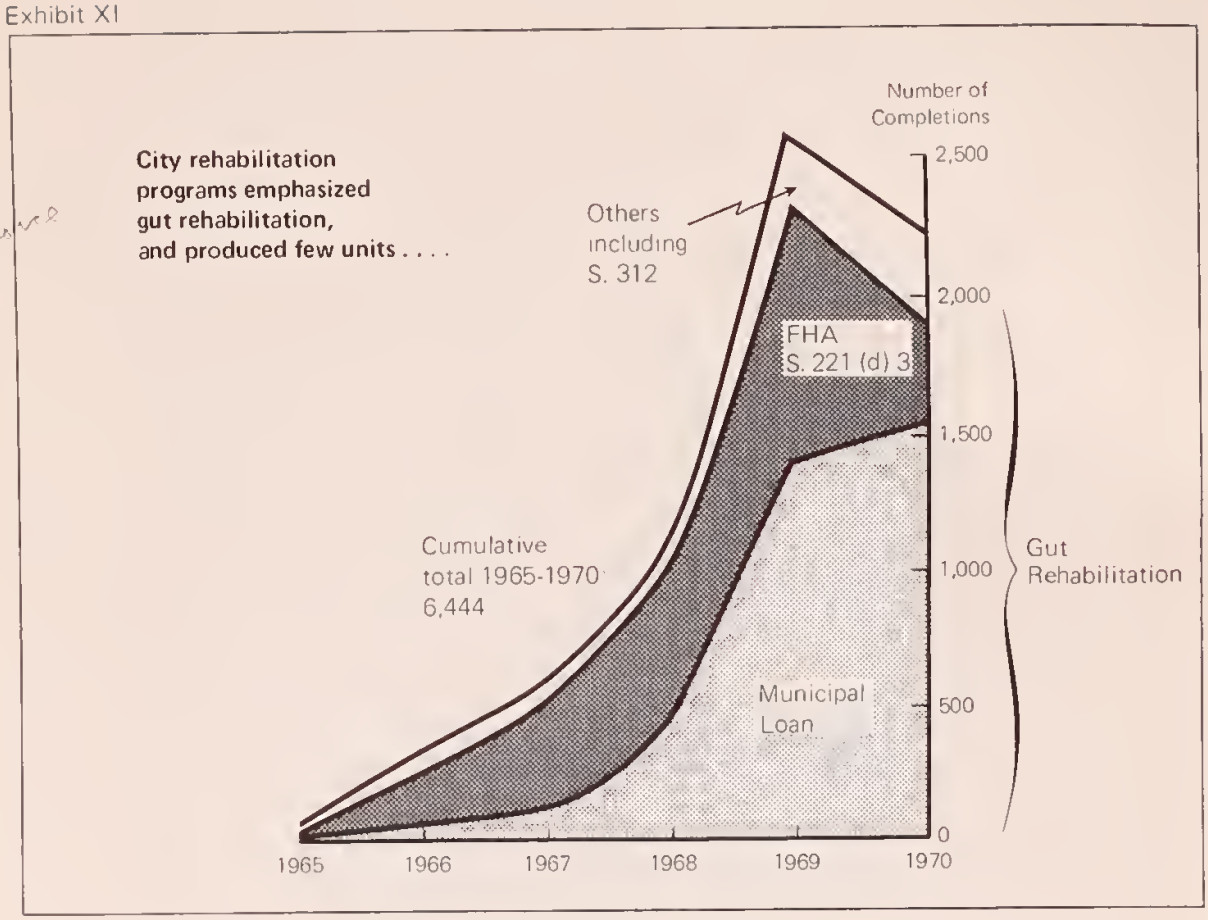
2. Rehabilitation. Four levels of rehabilitation can be undertaken (Exhibit IX), and the costs of rehabilitation vary significantly by rehabilitation level (Exhibit X). Given the rate of structural deterioration in housing, the rehabilitation needs of the stock were gigantic: $7.5 billion would have been needed to rehabilitate the stock in 1968. In contrast, given limited funds, the City's major rehabilitation programs produced a low number of units (Exhibit XI, on the next page).

   Rehabilitation programs are confronted by major policy dilemmas. The first is the choice between moderate rehabilitation (which, because of lower per unit costs, enables a larger number of units to be treated), and gut rehabilitation (which enables a lower number of units to be treated). The dilemma is created by the fact that gut rehabilitation can be targeted to core slum areas, where the need for improved housing is greatest; but because of the high costs, the postrehabilitation rental is so high that the original tenants of the housing cannot afford the rehabilitated housing. Moderate rehabilitation raises rents much less, but is appropriate only in less deteriorated buildings, hence generally in areas where income levels are higher.

   The City has been unable to resolve this problem to anyone's satisfaction. Its major rehabilitation programs, which involve mortgage financing and interest rate subsidies, have been targeted primarily toward gut rehabilitation in core areas (95 percent of all loans), and accordingly have achieved extremely low production rates. Moreover, the programs have been sufficiently scattered so that no significant effect on individual neighborhoods has been achieved; thus, private rehabilitation has not been encouraged, and the value of rehabilitation expenditures has been significantly reduced.

   In addition, the City has operated a tax abatement/exemption program (Section J51) since 1955, which provides for a 12-year exemption of any increase in assessed value due to building improvement plus an abatement of existing taxes up to 8.3 percent for 20 years. This program is poorly structured: It requires an absence of code violations (thus excluding buildings that most

Exhibit XI



need repair from the program); it provides no incentives to buildings with currently inadequate revenues; and it is available only for major capital improvements, not the kinds of repairs which are desperately needed by a majority of low-rent buildings. The program therefore targets better buildings in sound areas; provides assistance to buildings which would probably have been improved without this assistance; and overcompensates landlords for these improvements.

Thus, the City's rehabilitation efforts have been characterized by high costs, low program volumes, poor targeting, and, as a consequence, limited effectiveness in leveraging public funds by attracting complementary private rehabilitation.

3. Problem Buildings Programs. The City, in a belated effort to stem abandonment and deterioration, started several programs oriented toward evaluation, assistance or compulsion of owners to improve individual buildings. The Emergency Repair Program, initiated in 1962, provided for response to tenant complaints by pressuring the owner to make needed repair, and for City-funded repairs where emergency conditions existed. The Housing Repair and Maintenance program provided for the City to establish a contract with owners of buildings whose revenues were too low to permit immediate repairs, under which rents were placed in escrow and used to fulfill an agreed-on schedule of repairs over time.

   In 1962, the Receivership Program was initiated, enabling the City to take over management and control of a seriously deteriorating multiple-dwelling unit, to make repairs required to remove all violations, and to return the buildings to the owner once the City's costs have been recovered. In practice, many owners have abandoned these buildings and the City has become the owner through the In-Rem Program - between 1962 and 1966, the City became the owner of 117 buildings in this way. Problems in disposing of these buildings became acute and the program was curtailed from 1966 to 1970.

In sum, the City's housing programs have suffered from the inability to counter large-scale deterioration of housing in a severely difficult housing market situation, and from a number of inadequacies in program structure. In the period to 1970, therefore, they had little overall impact, and the structural deterioration of housing proceeded apace. Major problems included inadequate funding of these programs, lack of an adequate building information and evaluation system, consequent lack of program coordination and control - in short, the City's failure to develop an overall plan for housing conservation.

Essential Services

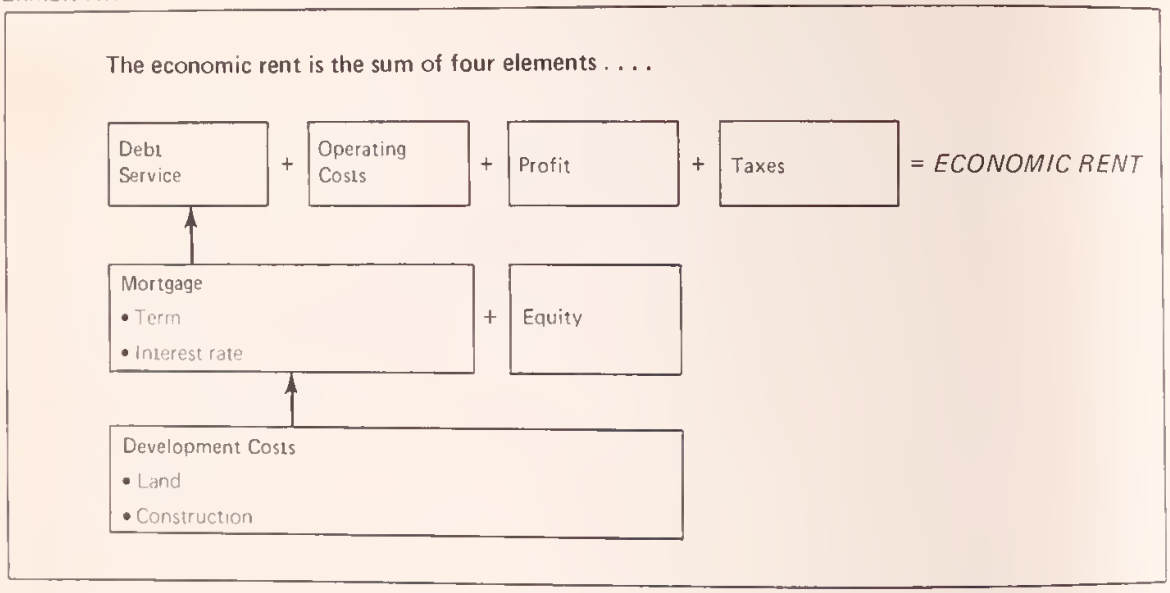
A second way to look at the quality of housing enjoyed by the City's residents is to examine the experience with the provision of essential housing services - primarily heating and hot water. Under rent control, the City has maintained a program to reduce rents where tenants can prove that essential services are not being provided. The number of such complaints grew from 133,000 in 1965 to 478,000 in 1970. While many of these complaints were resolved by the restoration of services, in 10 percent of the cases, rent reduction actions were completed. This is partial evidence of a serious decline in housing services.

Both housing deterioration and the decline in housing services during the 1960s were the products of serious constraints on building revenues, which were in turn caused by a combination of rent controls and tenant poverty.

THE PRICE OF HOUSING SERVICES

The standard of housing quality that is considered acceptable has risen consistently over the past two decades; the costs of maintaining that quality have risen even faster. Accordingly, the "economic rent" - the rent level that is required for a property owner to service his mortgage, pay his taxes, maintain the property and earn a competitive return from his property investment - has risen over time. (The concept of the economic rent is illustrated in Exhibit XII.)

Exhibit XII



If rents are held below economic rent levels, the property owner will be unable to fulfill all his financial obligations, and will look for ways in which to reduce his expenditures. Since the component of expenditures which is most easily reduced is repairs and maintenance, this will decline fast - with a resulting decline in housing quality.

If, on the other hand, actual rents rise toward the level of economic rents and keep pace with inflation, while incomes do not rise proportionately, housing maintenance will be adequate but tenants will have inordinate rent expenditures to secure this level of housing quality. If actual rents rise

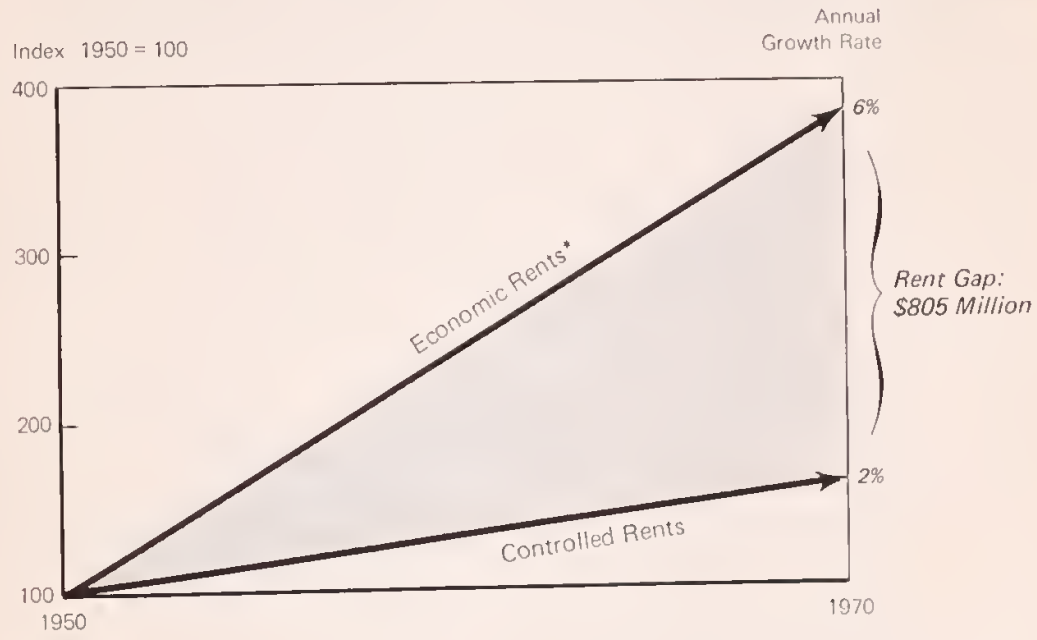
faster than incomes, but slower than economic rents, tenants will suffer both a decline in housing quality and an increase in rent burdens.

The central dilemma facing the City in the 1960s became the appropriate distribution of inflated housing costs between landlords, tenants, and the public treasury. The City's response - the continuation of rent control, applied and maintained since 1943 - produced the following major results.

Rents rose much slower than operating costs. Over the period 1950 to 1970, rents rose only 2 percent annually, while operating costs rose 6 percent annually (Exhibit XIII). This fundamental cost-price squeeze is the root cause of the City's housing deterioration.

Exhibit XIII

Between 1950 and 1970, economic rents rose faster than controlled rents, resulting in a rent gap of $805 million . . . .



** As measured by the MBR formula.*

By 1970, the rent gap was about $805 million. The rent gap - the difference between the rents landlords were actually receiving and the rents required to maintain their properties adequately - widened throughout this period.*

Moreover, serious inequities existed both among landlords and among tenants. The old Rent Control Law granted rent increases based primarily on apartment turnover. Since this was an accidental basis, similar apartments rented for very different rents. Moreover, buildings varied widely in the relationship between actual rents and the rents required for decent maintenance, as shown in the following table.

Table 2

Percentage of Buildings by Rent Gap

Percentage of Buildings	Gap Between Economic and Actual Rent
4.2%	No gap
8.9	0-15%
17.2	15-30%
33.3	30-45%
46.4	Over 45%

Among tenants, as shown in Exhibit XIV, the inequities were marked and were of two types:

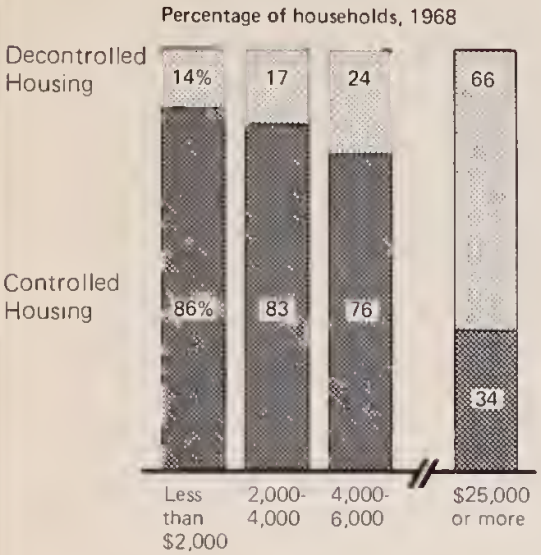
- Tenants at the same income level paid very different rents depending on whether they were in controlled or uncontrolled housing and, within controlled housing, depending on their tenure.

- Many high-income tenants, who could have afforded higher rents, received unnecessary rent protection while lower-income tenants were bearing disproportionate rent burdens.

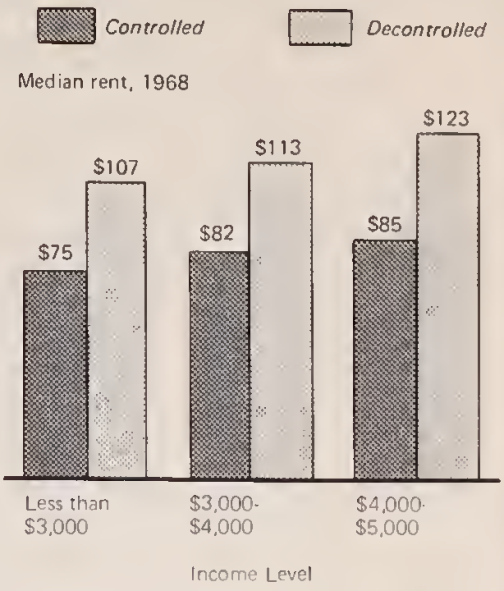
* - This calculation takes 1972 MBR levels as the standard against which the rent gap is calculated. Market rents were considerably higher than MBR rents.

The old rent control system resulted in serious inequities among tenants . . . .

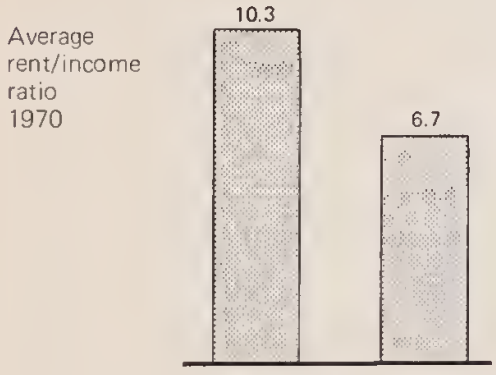
Many low-income households were unable to locate controlled apartments . . .



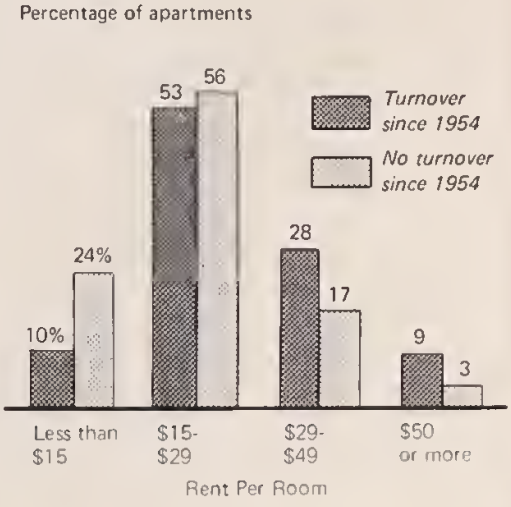
. . . And paid much higher rents in decontrolled apartments . . .



Meanwhile, rent control subsidized many high-income households . . .



. . . And rents for similar apartments varied substantially because of turnover . . . .



Because of rent control, the City was involved in making thousands of detailed apartment-by-apartment decisions. For example, the City operated a series of provisions enabling rent increases or reductions within the control framework. These required a large bureaucracy to maintain records, process papers, and conduct hearings and other actions. Moreover, both landlords and tenants refused to deal with each other directly and concentrated on the City bureaucracy as the prime target of their actions and frustrations; the political dilemmas became acute and paralyzed the bureaucracy.

* * *

In summary, the housing available to City residents improved substantially over the period 1950 to 1965. From 1966 onward, however:

- The housing stock declined in total, at a rate of approximately 9,500 units annually.
- The sound housing stock declined even faster.
- For this declining quantity and quality of housing, low-income tenants paid an inordinate share of their incomes.
- Landlords, faced with a rent gap of $805 million, began to withdraw from rental housing in the City. This withdrawal showed up, not primarily in lower rates of new construction, but in massive deterioration and abandonment of the existing stock.
- At the same time, landlords and the City were subsidizing a large number of upper-income tenants who could have afforded to pay higher rents.
- City programs were proving wholly inadequate to mitigate the severe housing crisis.

2 - Government's Response to the Housing Problem

In the early 1970s, faced with a growing list of housing problems, particularly the massive deterioration in the housing stock, the City administration substantially revised the emphasis and operating procedures of many of its housing programs and introduced a number of wholly new programs. The major program innovations undertaken during this period are listed in Exhibit XV. In this chapter, we describe the provisions and rationale of each of these new housing programs, and then evaluate recent evidence of their impact on the quantity, quality, and rents of the City's housing.

CHANGES TO RENT CONTROL

By 1970, a series of studies had provided stark evidence that the root cause of housing deterioration in the City was the existence of a large and growing "gap" between actual rents collected by building owners and the rents required to cover the growing costs of operating and adequately maintaining the buildings. In addition, it was becoming increasingly clear that the traditional system of rent control - which based rent increases primarily on the rate of tenant turnover in apartments - had not only held average rents well below economic rents, but had also created major inequities among tenant groups. Tenants were faced with divergent rents for similar apartments, and low-income tenants were often paying high rents while upper-income tenants with long tenures were being protected from rent inflation.

The revised rent control system. Accordingly, a new system of rent control was legislated in 1970. This new system was to be implemented in two steps - a one-time special rent increase, designed to provide landlords with some immediate financial relief, to be followed by the introduction of a new procedure for determining controlled rents which would gradually move rents toward an "economic" level and reduce the present inequity among tenant groups and building owners.

The special rent increase program had three major provisions:

SUMMARY OF RECENT PROGRAM INNOVATIONS

HOUSING PROBLEM	PROGRAM INNOVATIONS
Rent gap	Rent control reform – MBR program Vacancy decontrol of apartments under Rent Control and Rent Stabilization
Deterioration of existing housing	Tying of Code Enforcement and Essential Services to MBR rent increases Expansion and consolidation of Problem Buildings programs Decentralization of HDA programs; new neighborhood preservation focus Rehabilitation Mortgage Insurance Corporation
High rate of abandonment	Acceleration of City take-over of buildings City-assisted low-income cooperative ownership
Declining rates of new construction	Section 421 tax abatement Housing Development Corporation
Ineffective legal procedures	Housing Court

1. Allowable rent increases were scaled inversely to the number of previous rent increases. Apartments which had received two or more 15 percent increases since 1953 received no rent increase; apartments which had received one 15 percent increase since 1953 were allowed to raise rents by 8 percent; and apartments with no previous 15 percent increases were allowed a 15 percent increase. Apartments renting for under $60 per month were allowed increases of $10 or $15, depending on their size. All apartments were allowed rent increases necessary to recoup recent additions to labor costs.

2. Increases were subject to revocation unless the landlord could certify that: (a) he was spending for building operation and services an amount equal to his average expenditures in the previous 5 years plus 90 percent of the interim increase collected; (b) he had corrected all major (rent impairing) housing code violations and 80 percent of other violations; and (c) he was maintaining all essential building services.

3. The elderly poor were exempted from the increases. Persons exempted were those over 62 years of age, with annual incomes of less than $4,500 and with rents which were over a third of their disposable incomes.

Based on a sample of rent increase applications submitted in 1970, we estimate that the first-year increase produced an additional $85 million in building revenue, or an increase of about 7 percent in the controlled rent roll. About three-quarters of this additional amount was paid by tenants in apartments renting for under $100 per month - which were most in need of additional revenue but were also most likely to be occupied by low-income tenants. Approximately 23,000 elderly low-income households were wholly or partially exempted from the increase.

The permanent revisions to the rent control program were known as the Maximum Base Rent or MBR program. This program provided for calculation by the City's Housing and Development Administration of a maximum rent for each controlled apartment, using data on buildings and apartments submitted by landlords and verified by HDA. Four guiding principles were followed in developing the MBR program:

1. All buildings were to receive revenues adequate to provide for proper maintenance and to stem further deterioration. Revenues

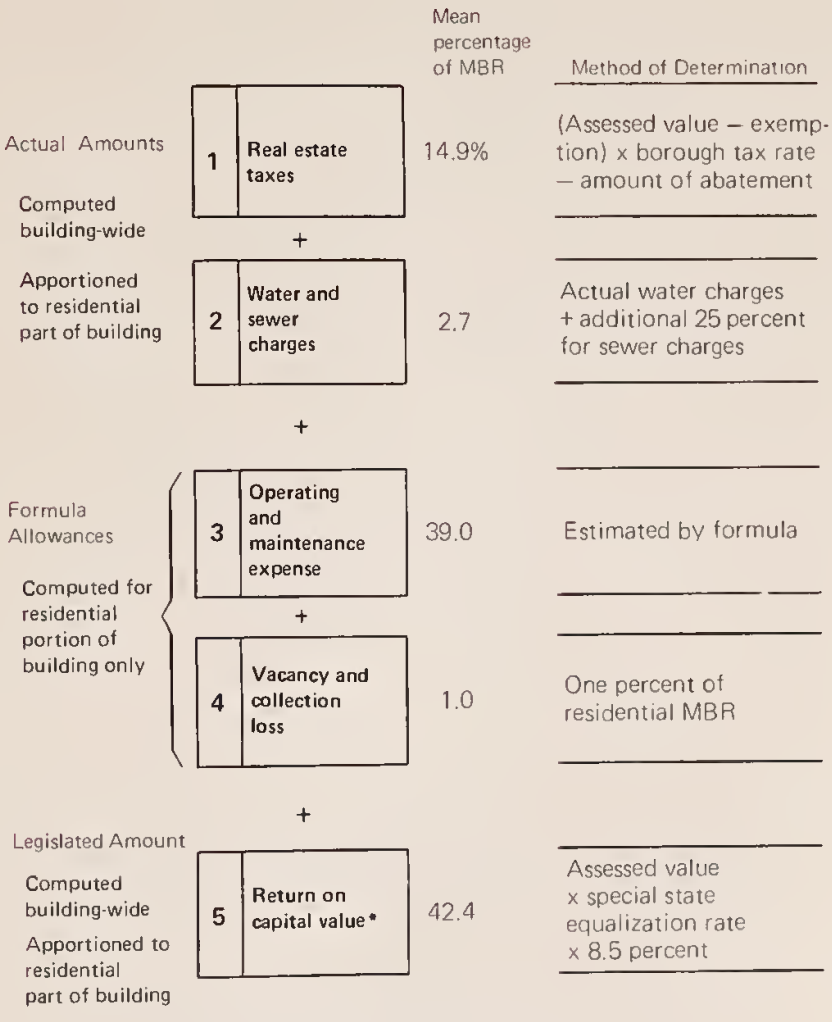
to landlords were to cover the full costs of operating and maintaining a building, including a competitive rate of return to the owner in order to prevent disinvestment in the building. Therefore, the MBR rent was to be computed as a summation of actual expenditures on certain verifiable items plus allowances estimated by formula for the expenditures required to maintain the building adequately and cover the building's financial commitments. Exhibit XVI shows the five components of the MBR rent and how they are calculated.

Real estate taxes and water and sewer charges are the actual amounts paid by the landlord. Operating and maintenance expenditures are estimated by means of a formula that takes into account such factors as the number of apartments in the building, the number of rooms, the age of the building, and the level of labor services provided. An allowance to cover losses from vacancies is computed as 1 percent of the rent roll (since this is the historical vacancy rate). And finally, the MBR rent includes an allowance to cover the debt service on the building and provide the landlord with a fair rate of return. This allowance was legislated at 8-1/2 percent of the building's assessed value multiplied by a special equalization rate (i.e., 8-1/2 percent of the approximate full value of the building). The allowance was estimated in this manner so that the City would not have to compute the exact amount of mortgage debt outstanding on each building.

2. Inequities between buildings and between tenants were to be reduced. Buildings with large gaps between revenues and expenditures would receive larger increases than buildings with smaller gaps. Similar apartments would have similar rents, and rents would vary rationally with apartment size and the quality of services provided.

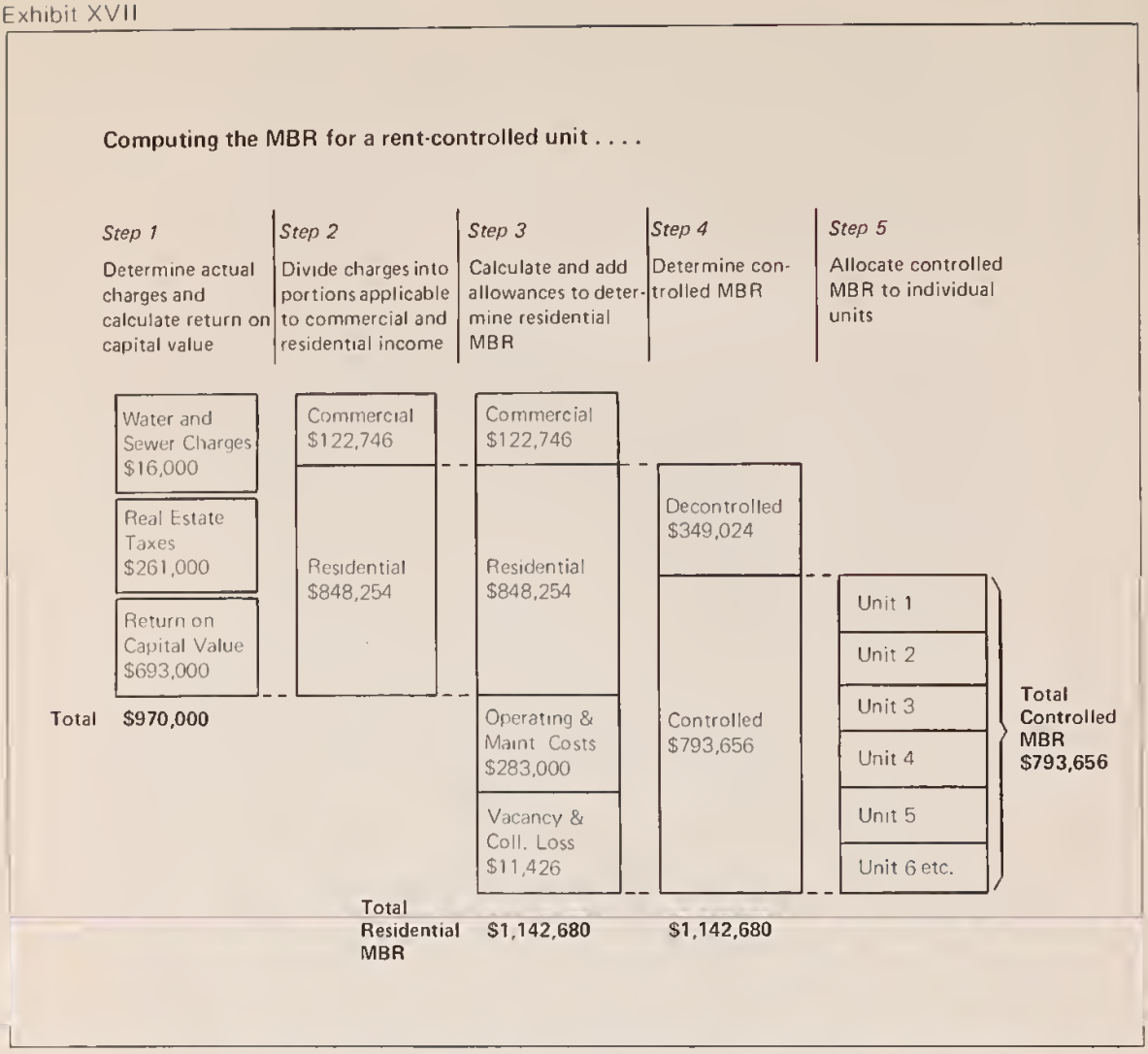
   The MBR was first to be calculated for the building (taking into account whether the building had commercial as well as residential income). This overall building MBR was then to be allocated to individual apartments, taking into account their size and floor location (Exhibit XVII). Apartments with current rents above their MBR would receive no rent increases; apartments with rents below MBR would receive gradual increases until they reached the MBR level. These provisions would thus begin to reverse the inequities that existed under the previous rent control system. Over time, similar apartments would approach similar rents; tenants already paying too much for their apartments would not

The MBR rent has five components . . . .



* *Includes an allowance for interest and amortization charges and profit.*

Exhibit XVII



pay more, and tenants with lower rents in relation to the size of their apartments would face rent increases. At the same time, the MBRs would constitute a ceiling on overall building revenue.

3. Tenants were to be protected from sudden, sharp rent increases, given the large size of the rent gap and large number of low-income households in the City. Accordingly, the program provided that rents could not be raised by more than 7-1/2 percent a year. However, rents for apartments that became vacant would jump immediately to their MBR levels.

4. Elderly, low-income tenants were to be exempted from rent increases. The 1970 rent exemption program was extended, and its terms were liberalized: The income limit for eligibility was raised to $5,000. Landlords were to be compensated for the amount of the rent increase from which tenants were exempted, through the tax abatement.

In order to prevent the reemergence of a large rent gap, with its deleterious effects on housing quality, the MBR program provided for the recalculation of maximum base rents every 2 years. Thus, the first round of MBRs were to be calculated in 1972; these would govern rent increases in 1972 and 1973. MBRs would then be recalculated in 1974.

The MBR program also provided for landlord certifications of maintenance of essential building services and removal of the majority of outstanding code violations, in order to be eligible for rent increases. The rent increases were to be linked to specific efforts under code enforcement and other programs to ensure that landlords actually used the increased revenues for improving building quality and services.

The Vacancy Decontrol Law. Vacancy Decontrol provided that, effective July 1971, rent-controlled and rent-stabilized apartments becoming vacant would no longer be subject to these programs: these apartments could then be rented at whatever market rent levels landlords were able to obtain for them. Vacancy Decontrol was enacted by the State Legislature over the objections of the City, which had less than a year earlier enacted the MBR law.

The Vacancy Decontrol law had two purposes: First, accelerate the rate at which collectible rents rose toward market rent levels, thus closing the rent gap faster than would have occurred under the MBR program; and, second, begin to dismantle all forms of rent control in New York City by reducing the proportion of the housing stock which would continue to be subject to controls. If the Vacancy Decontrol law were to remain in effect, normal tenant turnover patterns would eliminate rent control entirely in 7 to 10 years.

In 1970, the rent-controlled stock in New York City included approximately 1,265,000 apartments. All of these were theoretically eligible for

both the interim rent increase and the MBR program, although in practice it was expected that some low-rent buildings would find it not worth while to apply (because rents were limited by tenant incomes rather than by controls) or would be unable to meet the certification requirements of these programs. With the enactment of Vacancy Decontrol, apartments became decontrolled as current tenants moved out, thereby reducing the number of apartments under the MBR program.

The Rate of Decontrol

A recent survey of buildings which were rent controlled in 1970, undertaken by the City's Housing & Development Administration, shows that about 30 percent of apartments in these buildings had been decontrolled by November 1973.* (See Exhibit XVIII.) Thus, in less than 2-1/2 years, about 361,000 apartments have been decontrolled from the rent-controlled stock alone (this figure does not include the rent stabilized apartments which have been decontrolled). Not only is the Citywide rate of decontrol high, it is also accelerating: 11 percent of controlled apartments were decontrolled in the year ending October 1972, while an additional 16 percent were decontrolled in the next year.

Decontrol is occurring most rapidly in the Bronx, where 38 percent of the 1970 rent-controlled stock has been released from controls. This is primarily due to the composition of the Bronx population, which includes a high proportion of younger, relatively more mobile, single-person households (36.4 percent of the Bronx population is under 35 years old). By contrast, in Queens where the population is older and more stable (only 19 percent is under 35 years old, and almost 40 percent is over 65), the rate of decontrol has been much lower - only 22 percent.

Vacancy decontrol is proceeding in all types of housing. Of those tenants who were in the rent-controlled stock in 1970, the proportion who are now in decontrolled housing does not vary materially by income level. Twenty-six percent of low-income tenants formerly in rent-controlled apartments are now living in decontrolled apartments; this proportion rises to 33 percent for tenants earning between $8,000 and $15,000.

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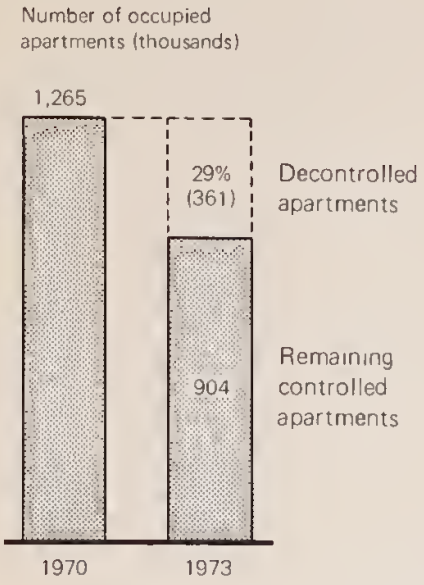
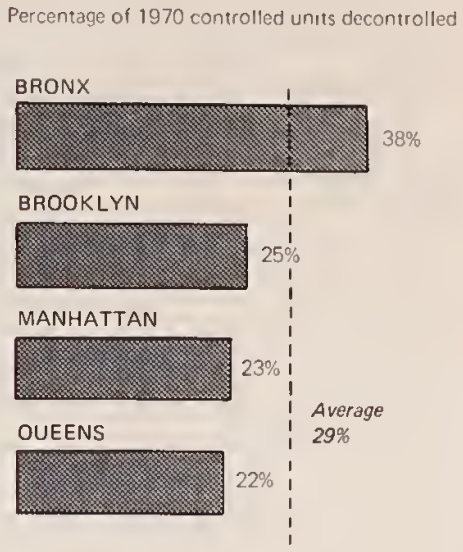
* - We are indebted to Andrew P. Kerr, former Administrator of the Housing & Development Administration, for providing us with the results of this survey.

The rate of decontrol is high and rising . . . .

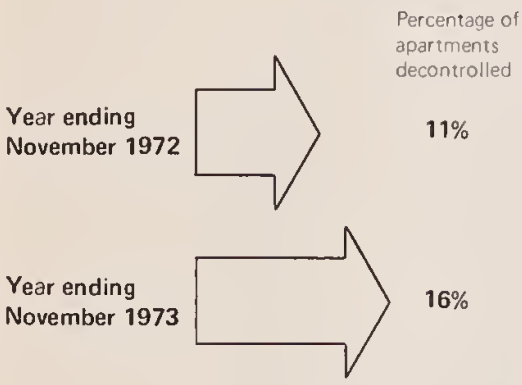
Since 1970, 29 percent of the rent-controlled stock has been decontrolled . . .



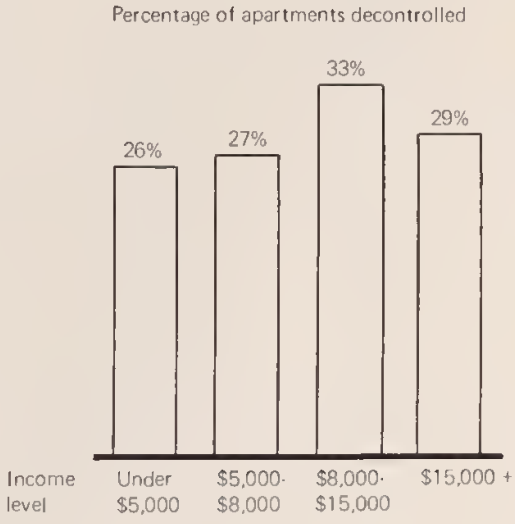
. . . With decontrol proceeding fastest in the Bronx . . . .



The rate of decontrol is accelerating . . . .



Decontrol has occurred at all income levels . . . .



The Impact on Rents

The combined impact of the Vacancy Decontrol and MBR programs on rents has been surprisingly large* (Exhibit XIX). The average rent-controlled apartment in 1970 rented for $107 a month. With the first-year increase and the MBR program, 1973 rents for still controlled apartments have risen on average to $143, an increase of 34 percent. Rents for decontrolled apartments have jumped to an average of $190, an increase of 78 percent. Overall, tenants who were in the controlled stock in 1970 have seen rents rise to an average of $157, an increase of 48 percent.

These rent increases have not been uniformly distributed across the housing stock. As would be expected, dollar increases have been higher for those apartments which had higher initial rents - these are the better apartments, with higher market rent levels, and with tenants who can more easily afford the increased rents. Nevertheless, the increases confronting even low-income tenants have been substantial. For example, the lower portion of Exhibit XIX shows that tenants with incomes below $5,000 have seen their rents increase from an average of $82 to $124 under the MBR program (up 51 percent), and all the way to $150 in decontrolled apartments (up 83 percent). This implies an average rent increase for low-income tenants from $82 to $134, or nearly 64 percent.

The Impact on Tenants

These rent increases have significantly outpaced growth in tenant incomes over the period 1970 to 1973. Accordingly, the percentage of tenant incomes necessary to secure housing in the City has risen, at all income levels.

Exhibit XX shows that low-income tenants (those receiving less than $5,000 a year) spent an average of over 41 percent of their incomes on housing in 1973 - a substantial increase over the 35 percent they were paying in 1970. Many of these tenants are on public assistance, so it is the welfare

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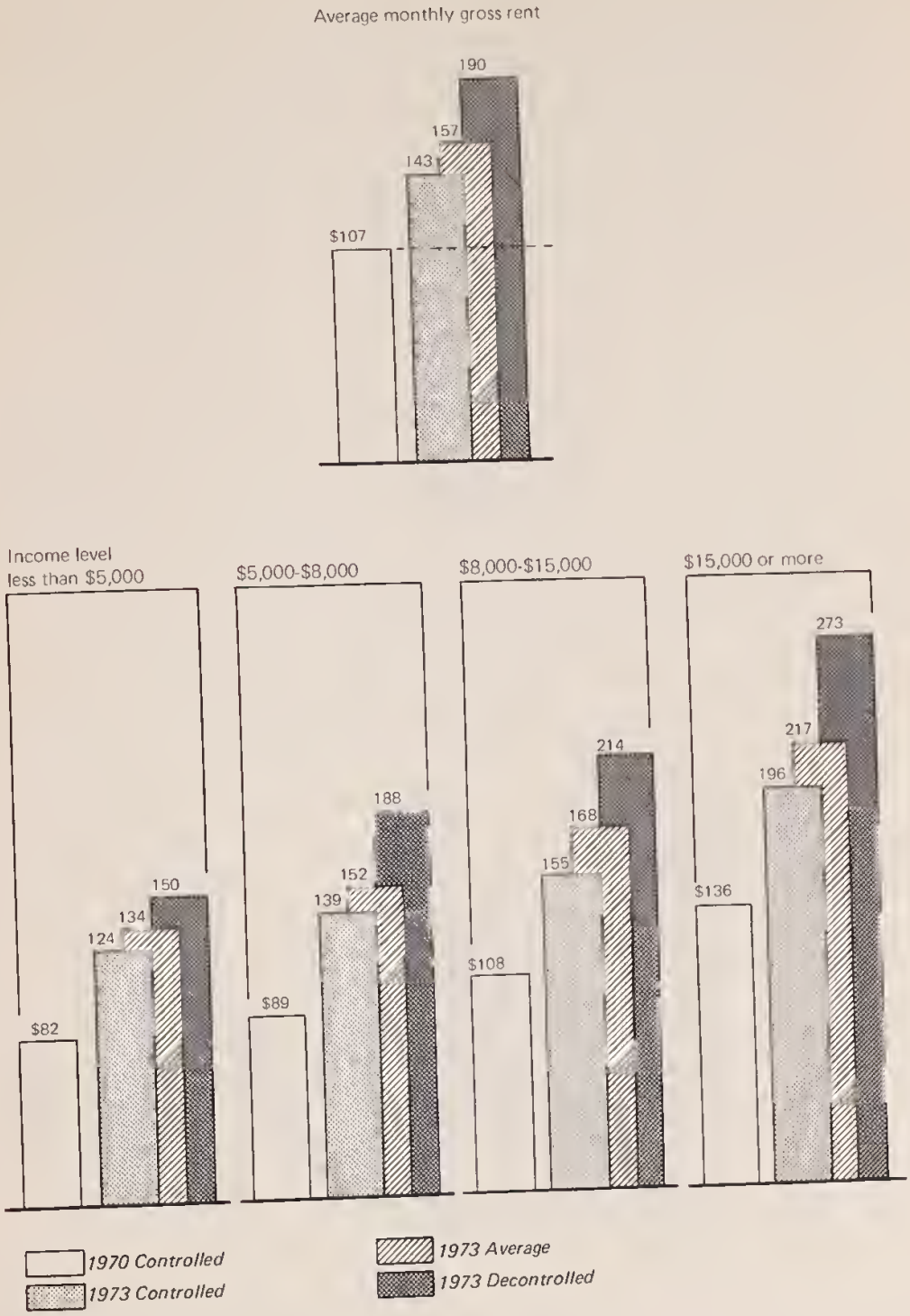
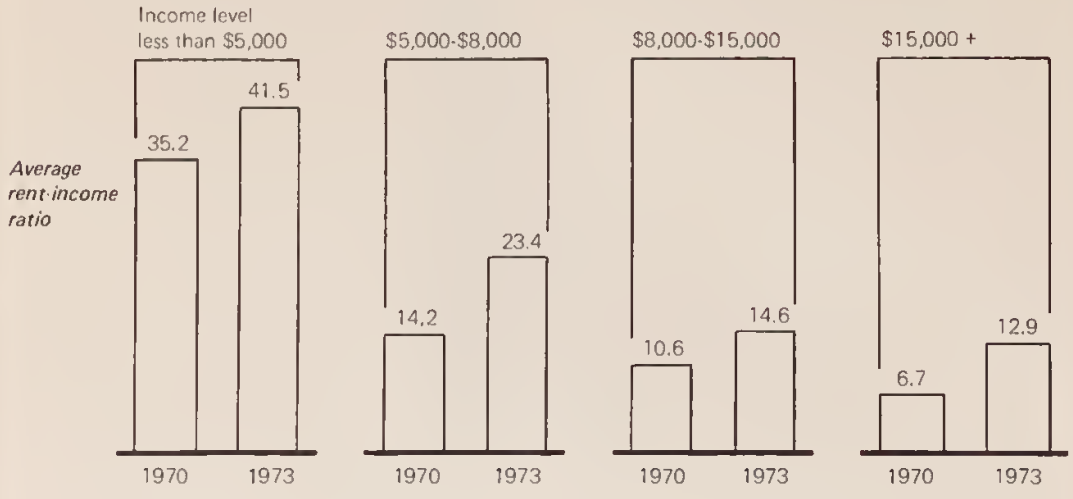
* - In the subsequent text and exhibits, "controlled" refers to the 904,000 apartments which were still controlled in November 1973; "decontrolled" refers to the 361,000 apartments released from the rent-controlled stock because of vacancy decontrol; and "average" refers to the combined impact of the two programs on the total 1,265,000 apartments which were rent controlled in 1970.

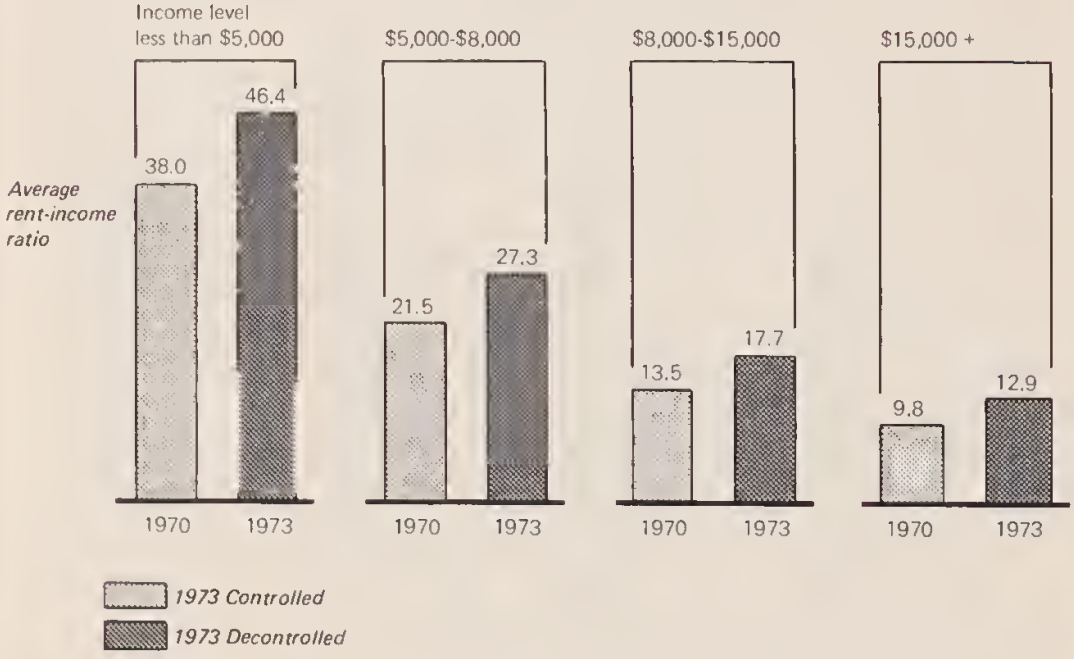
Both the MBR and vacancy decontrol programs have led to large rent increases . . . .



The percentage of income spent on rents has risen at all income levels . . .



. . . And rent-income ratios are higher for those in decontrolled housing . . . .



system rather than the individual which incurs the additional housing costs. Nevertheless, those tenants in this group who are not on welfare are seriously affected. And if a system of fixed welfare housing allowances is enacted in the future, welfare tenants will also be adversely affected.

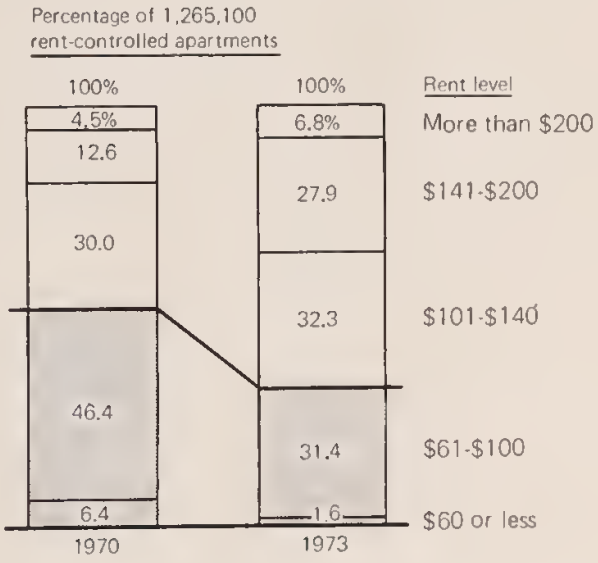
Tenants earning incomes in the lower-middle range, say $5,000 to $8,000, are even more severely affected by the Vacancy Decontrol and MBR programs. While their initial rent-income ratios were much lower - an average of 14.2 percent - they have experienced the largest relative increase, up to an average of 23 percent. For higher-income tenants, the percentage of income spent on rent has increased but continues to be significantly less than for tenants with lower incomes.

The Vacancy Decontrol law has led to another form of inequity: rent-income ratios within a given income group now vary substantially depending on whether tenants are in controlled or decontrolled housing. Thus, tenants earning under $5,000 a year who move into decontrolled apartments can now expect to pay around 46 percent of their incomes for housing, compared to 38 percent if they stay in controlled housing (Exhibit XX).

The significance of these developments for low-income tenants can be assessed in another way - by examining the number of low-rent apartments still available in the City. As Exhibit XXI shows, the percentage of apartments renting for under $100 per month has declined from 52.8 percent to 33 percent. This is significant primarily because households with

Exhibit XXI

The percentage of low-rent apartments has declined dramatically . . . .



incomes of under $5,000 tend to include the types of persons whose opportunities to increase their incomes are low - either because they have limited skills and access to employment or because they are on some form of public assistance, which increases rather infrequently. Thus, for this group especially, Vacancy Decontrol and MBR together will continue to raise the proportion of their incomes which must be expended on housing and will continue to constrict their nonhousing expenditures accordingly.

We do not wish to exaggerate the impact of these two programs on tenants. Rent increases were clearly necessary to reduce the rent gap, and the impact on tenants was foreseen when the programs were legislated. The rent increases have reduced at least one form of inequity among tenants - namely the implicit subsidies to high-income tenants which were provided by the old rent control system. Moreover, the MBR program has undoubtedly reduced the disparity in rents for similar apartments and buildings (although Vacancy Decontrol has presumably increased rent skewing). Nevertheless, the combined impact of these programs on tenants with low incomes who are not protected by any form of public assistance has been severe and will continue to be so unless ameliorative action is taken soon.

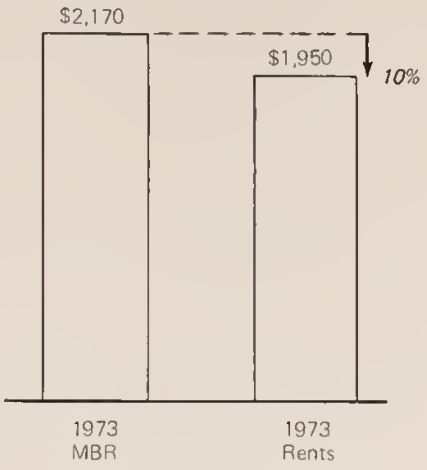
The Impact on the Rent Gap

To what extent have the rent increases under MBR and Vacancy Decontrol achieved their purpose of filling the rent gap and stemming housing deterioration?

The rent gap was calculated as the difference between actual rents collected for the controlled housing stock in 1970 ($1,365 million) and the rents that would have been required to cover all housing costs and provide for an adequate level of maintenance ($2,170 million), as measured by the MBR formula. As Exhibit XXII shows, rents rose sufficiently in the period 1970 to 1973 to close 73 percent of this rent gap of $805 million. The first-year increase amounted to $85 million. Increases under the MBR program were in the order of $150 million, slightly lower than the $177 million which had been projected to occur in 1972 and 1973. Vacancy Decontrol, on the other hand, enabled rent increases of approximately $350 million; decontrol alone was responsible for closing 43 percent of the rent gap. Altogether, revisions to rent control have raised the rent roll for the 1970 controlled stock to $1,950 million - only 10 percent below the $2,170 million that was considered a fully adequate aggregate rent in the City in 1973. This represents a much larger increase in collected rents - and, consequently, a much more rapid closing of the rent gap - than most housing analysts had expected.

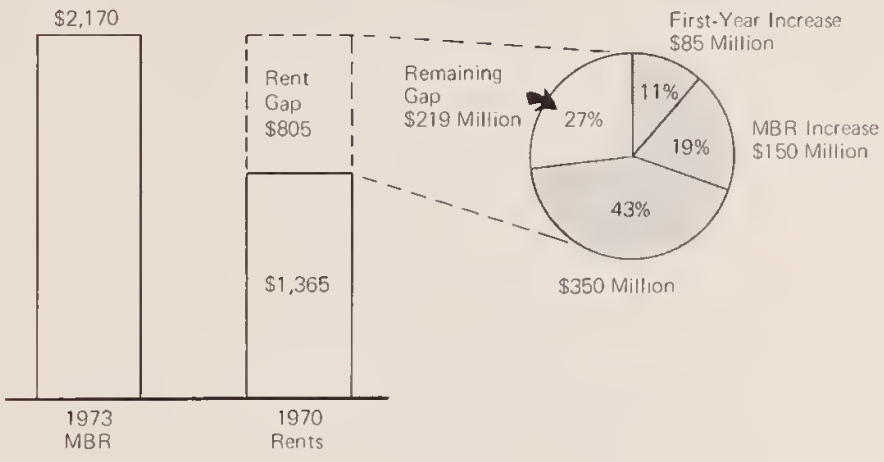
On average, rents are still 10 percent below MBR levels . . .

Rent roll for 1,265,000 controlled apartments
(Millions of dollars)



. . . But 73 percent of the rent gap has been filled . . . .

Percentage of rent gap filled



Because both housing costs and collected rents change from year to year, the rent gap turns out to be a moving target. It is worth examining how large this gap will likely be in 1974 and 1975 as a critical consideration in the determination of future rent control policy. The size of tomorrow's rent gap will be affected by four factors: First, the recalculation of MBRs in 1974 will increase the gap. Second, rent increases in the controlled stock will decrease the gap. Third, rent increases under Vacancy Decontrol will further decrease the gap - and how fast this will occur depends on how fast apartments turn over in the future. Fourth, any adjustment to the formula by which MBRs are computed will increase or decrease the gap. An adjustment to the MBR formula could be argued for on two grounds: (1) that fuel costs have been increasing rapidly over the past several months, and this extraordinary cost increase should perhaps be passed on to tenants; and (2) that the unintended effect of the original MBR formula has been to provide an overly generous rate of return to owners, so that the MBR should be adjusted downward to provide a more normal rate of return. Following, we will discuss each of these factors in turn, project their impact on the size of the rent gap, and examine the implications of these projections.

Rent increases under the MBR program and Vacancy Decontrol had reduced the rent gap by the end of 1973 to about $219 million. In 1974, the recalculated MBRs will be raised by approximately $174 million, thus increasing the gap to $393 million. However, offsetting this will be an increase of controlled rents in early 1974 amounting to about $80 million. In addition, if Vacancy Decontrol continues at the same pace as occurred during 1971-1973, and decontrolled rent increases average the same as they did during that period, by the end of 1974, decontrol will have raised the rent roll by another $210 million. The net result of these various changes will be to reduce the rent gap to about $100 million in January 1975, as shown in Table 3.

Table 3

Projected 1975 Rent Gap
(Millions of Dollars)

Rent gap, November 1973	$219
1974 increase in MBRs	174
Rent gap, January 1974	*$393*
1974 controlled rent increase	$ 80
1974 Vacancy Decontrol rent increase	210
Remaining rent gap	*$103*

Two possible adjustments to the MBR formula - which provides the standard against which the rent gap is calculated - should also be considered.

First of all, the recent impact of the energy crisis has been to considerably raise fuel costs for apartment buildings. According to cost indexes constructed by the Bureau of Labor Statistics for rent-stabilized buildings, and appropriately modified to represent more accurately the characteristics of rent-controlled buildings, fuel and utilities constituted approximately 21 percent of total operating and maintenance costs in 1972. Since operating and maintenance costs are, on average, 40 percent of MBR rents, fuel represents about 8 percent of these rents. Fuel costs have risen at least 25 percent on the average and as much as 60 percent in some cases since 1972. If we assume that heating oil costs in 1974 will be 60 percent on the average above their 1972 levels, this would require an increase of, at most, 5 percent in the controlled rent roll. (In fact, the required increase would be less, since some part of the fuel cost increase since 1972 is already taken into account in the 1974 recalculation of MBRs.) A "passalong" of increased fuel costs would thus require a total rent increase of about $100 million.

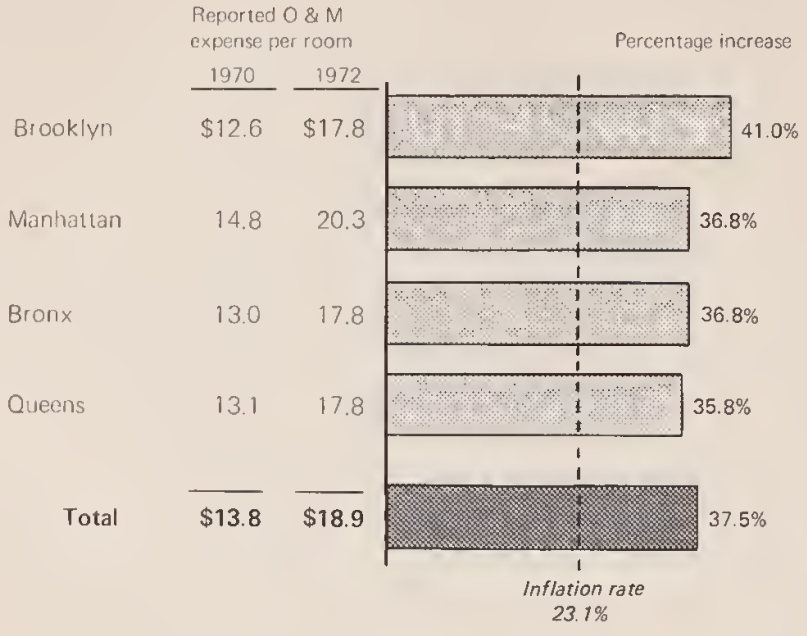
More than offsetting this adjustment to the MBR rent levels is a possible downward adjustment in the Maximum Base Rent formula to reduce the return on capital value afforded the building owner. This component of MBR rents is supposed to provide for both debt service on the mortgage and a reasonable rate of profit. It was legislated as 8-1/2 percent of the building's assessed value multiplied by a special State equalization rate (which is supposed to represent the amount by which the building's assessed value must be raised to approximate market value). Evidence suggests that the special equalization rate is too high - primarily because it is computed on a base which includes both commercial and residential properties - and that the return on capital value component, therefore, overcompensates landlords. The impact of this overcompensation is increased by the fact that about 20 percent of rent-controlled buildings do not have any outstanding mortgage debt at all, so that the return on capital value component provides a profit of 8-1/2 percent on an inflated market value of the building. Reducing this rate of return - or adjusting the equalization rate - would reduce 1974-1975 MBR rents by about $130 million for still controlled apartments.

This last argument certainly does not mean that landlords are making exorbitant profits now. The rents they now receive are still 10 percent below 1972 MBR rent levels, and reports from landlords indicate that they are spending the entire MBR allowances for operating and maintenance costs. These reports imply that landlords are either not fully servicing their debt or are making a below normal return on their investment.

The HDA survey shows that, between 1970 and 1972, operating and maintenance expenditures increased 38 percent Citywide although, since costs increased 23 percent, the real improvement in maintenance was much smaller (Exhibit XXIII).

Exhibit XXIII

Reported expenditures on housing operation and maintenance increased by 38 percent between 1970 and 1972 . . . .



If these reported O & M expenditures are correct, they imply that landlords of still-controlled buildings were receiving only a small portion of their return on capital value allowance, as shown in Table 4.

Table 4

1972 MBR Allowance and Actual Receipts (Manhattan)

	Per Room		Percentage of ROCV Allowance Received
	MBR Allowance	Actual	
Rent	$50.3	$43.8	
Operating expenses	28.8	28.8	
Return on capital value	*$21.5*	*$15.0*	69.8%*

** Brooklyn 31.4 percent; Bronx 42.1 percent; Queens 71.0 percent.*

However, this situation will be altered once further rent increases under the MBR and the Vacancy Decontrol programs fully close the rent gap. If no changes are made to these programs, the rent gap will be fully filled by mid-1975 (including the fuel cost passalong) and, at that time, landlords will be receiving a high rate of return on capital value. The projections underlying this conclusion are summarized in Table 5.

Table 5

Projected Rent Gap With No Change in MBR or Vacancy Decontrol
(Millions of Dollars)

	1974	1975
Rent gap		
Beginning-of-year rent gap	219	100
Increase in M8Rs	174	–
Increase in fuel costs	100	–
Total rent gap	*493*	*100*
Rent increase		
Controlled rent increase	80	65
Vacancy Decontrol increase	210	190
Fuel cost passalong	100	–
Total	*390*	*255*
Remaining rent gap	103	(155)
Adjustment for ROCV	(130)	
Adjusted rent gap	*(27)*	

If the MBR formula were modified to reduce the return on capital value to a more normal level, the rent gap would be entirely eliminated by the end of 1974. In other words, by the end of 1974, most landlords will be receiving revenues adequate to cover their operating expenses and earn a reasonable rate of return. If the MBR and Vacancy Decontrol programs are continued in their present form, building owners will begin to be overcompensated, while rent burdens on low-income tenants will be increasing unnecessarily. As we argue in the next chapter, the MBR and Vacancy Decontrol systems can now be substantially modified to attain equity among landlords and tenants without inviting further large scale deterioration of the housing stock.

EFFORTS TO IMPROVE HOUSING SERVICES

With the implementation of the MBR and Vacancy Decontrol programs, both of which addressed the shortage of rental revenues, the City began to strengthen and coordinate a variety of programs directed at ensuring that rent increases were translated into improvements in housing quality. Some of these program innovations are too new to have had any measurable impact as of this writing. However, in the following sections we provide some partial evidence of whether services from the existing stock have begun to show any improvement.

Tenant complaints about decreases in essential services provide a partial indicator of the quality of housing services being offered. In 1971 - after the interim rent increase - 344,000 complaints for decreased services were received by HDA. Of these, 42,000 or about 11 percent were of sufficient validity to warrant rent reductions (in 18,000 cases, services and rents were subsequently restored). In 1972 - after the first round of MBR increases - 333,000 complaints were again received, of which almost 70,000 led to rent decreases. The explanation for such high figures is threefold. Some of the decreases represent an inability to raise rental revenues sufficiently to maintain services, despite increases in legal rents. In other cases, however, services decreased despite rent increases; and in some unknown number of cases, they represented attempts to harass or induce tenants to move (thus making the apartment eligible for vacancy decontrol). Whichever is the primary causal factor, these figures do indicate continuing deterioration in the quality of housing services available to the City's population.

Code Enforcement

The Code Enforcement effort was emphasized by explicitly linking it to rent increases under the MBR program. In order to be eligible for MBR rent increases, landlords had to certify that they had removed all rent-impairing violations and 80 percent of all other violations. Since the rent increases could not be granted until after the violations had been corrected, landlords unable to make this certification could sign an agreement with HDA's Office of Special Improvements, deposit their rents in escrow, and undertake a scheduled program of repairs and maintenance. Default on the agreement would bring revocation of the rent increases. (Later, the Office of Special Improvements was reorganized into the Office of Evaluation and Compliance, combining the MBR code violation certification activities with the Receivership and Housing Repair and Maintenance programs.)

The effort to link rent increases and code violation removal procedurally has proved to be a massive failure. The task of requesting, receiving, processing and evaluating certifications from 79,000 buildings - all with a single deadline - proved to be impossible for HDA. The violations certification procedure tied up countless inspection and processing man-days, significantly added to the burden of checking for MBR eligibility, delayed the issuance of rent increase orders, and led to widespread confusion and acrimony on the part of both landlords and tenants.

All this would have been worth while had these efforts led to structural improvement in the housing stock. But, in 1972, an additional 481,000 violations were reported, and only 280,000 violations were removed. Thus, in 1972 - the year when 80 percent of all violations were to be removed - the number of outstanding, uncorrected violations increased from 760,000 to 961,000. While some of this increase undoubtedly resulted from increased inspectional activity rather than any real change in the condition of the housing stock, it does indicate that the linkage of Code Enforcement to the MBR system served little purpose indeed. Moreover, the experience seems likely to replicate itself in 1974: by June 30, 1973, the deadline for certification for the 1974 MBR increases, only one-third of 78,000 rent-controlled buildings had returned completed certifications.

Neighborhood Preservation

Because of the abundant evidence that deterioration of the housing stock had been highly correlated with the process of neighborhood decline during the 1960s, the City began to reorient its programs and procedures to facilitate the concentration of preventive and corrective action on individual

neighborhoods which were deteriorating but could be saved. Transitional areas were to be selected on a variety of criteria - adverse housing stock indicators (high number of code violations, large number of buildings with tax arrears or mortgage foreclosures, a large number of buildings requiring emergency vacancy of tenants), shifts in population composition, or a major reluctance on the part of lending institutions to make mortgage loans for new construction and rehabilitation.

In these areas, which would typically border on major action areas or contain isolated pockets of deterioration within primarily sound areas, a local HDA administration was to be established. The local Area Coordinator would then use Code Enforcement (emphasizing cyclical rather than complaint-oriented inspections), receivership, Housing Repair and Maintenance, emergency repairs, together with funding from other programs such as Section J51 Tax Abatement/Exemption, Federal Section 312 and 115 rehabilitation loans, and Section 23 Public Housing leasing, in a coordinated attempt to stem further housing deterioration. The areas initially selected for this concentrated attention were Crown Heights and Bushwick in Brooklyn, Washington Heights and Clinton in Manhattan, and West Tremont in the Bronx. It is obviously too early to evaluate the impact of these concentrated programs; however, the basic premise of concentrating effort on a limited geographical area is certainly sound.

Ownership Change

The rent control revisions were partly aimed at providing landlords with sufficient revenue growth to prevent building abandonment. Problem buildings programs were also strengthened to identify and assist owners on the verge of abandonment. In addition, the City introduced an innovative program of "ownership change" or low-income co-oping, providing for the transfer of buildings from current owners to low-income tenants. This program has also included financial assistance for building rehabilitation and "sweat equity" participation by tenants. The program, funded at a level of $8 million, has so far financed the renovation of 17 buildings with 531 units; another 82 buildings with about 1,800 units are at various stages in the processing pipeline. The ownership change program emphasizes moderate to gut rehabilitation, but with sweat equity participation, unit costs are $5,000 to $7,000, instead of the more usual $14,000 to $16,000 for similar work on other units. The ownership change program shows great promise for the future.

Housing Court

Finally, in order to improve the City's enforcement of corrective actions by landlords, both by enabling coordination of diverse actions against individual building owners and by speeding processing of cases, the Housing Part of the Civil Court was established. The Court can deal with issues such as code enforcement (imposition and collection of penalties), injunctions and restraining orders (for example, to prevent evictions), recovery of City expenditures incurred in code violation removal and sealing and demolition of buildings, rent escrow, and receivership actions. The Court can enforce City liens against buildings and levies upon rents, to collect any civil penalties assessed.

The major advantages of the Housing Court were expected to be the ability to consolidate all actions against one building, consider them together, act accordingly, and retain jurisdiction over the case until compliance was obtained. This consolidation, together with the reduction of delays, would greatly increase the effectiveness of governmental actions to compel landlords to improve their buildings.

While the establishment of the Housing Court is a major first step in the direction of improved enforcement, the procedures still place great reliance on the City's Housing and Development Administration to negotiate with landlords and tenants, to introduce compliance actions in the court, and to enforce court directives. The usefulness of the Housing Court could be greatly increased if it were seen as an instrument for encouraging landlords and tenants to bargain directly with each other and to reduce their reliance on the City bureaucracy. This change could be achieved by modifications to landlord/tenant laws which would improve tenants' access to bring certain cases directly to the Court. A number of such proposals are discussed in the next chapter.

* * *

In summary, despite increasing emphasis in City housing programs on the existing stock, little material improvement in the quality of housing services appears to have occurred since 1970. As we shall argue later, more funds for enforcement programs and improved procedures will have to be provided if the housing stock is to be significantly improved.

NEW CONSTRUCTION AND REHABILITATION

Three major programs instituted since 1970 have been aimed at reversing the decline in the size of the housing stock which has been occurring since 1966. First, Vacancy Decontrol and MBR should have raised new construction rates, by raising landlord expectations with respect to the rate of return they could hope to earn on these investments. At the same time, by providing revenues to the existing housing stock, these programs should have prevented some abandonments which would otherwise have occurred. Second, the Housing Development Corporation was intended to provide an additional source of financing for new construction, and also to lower rent levels for new housing through its below market interest rate program. Finally, a new tax abatement/exemption program (Section 421) was intended to provide a mechanism for lowering market rents and thus improving the marketability of newly constructed housing.

None of these objectives has been achieved. Table 6 shows the rate of housing completions and demolition for the years 1971 and 1972, compared to the average annual rates of these flows in the period 1966-1970.

Table 6

Flows Affecting the Housing Stock, 1971-1972

	Number of Units		
	Annual Average 1966-1970	1971	1972
New construction completions	22,750	19,460	22,110
Net conversions	1,120	940	(130)
Net additions	*23,870*	*20,400*	*21,980*
Demolitions	9,800	14,760	13,080
Net change in stock	*14,070*	*5,640*	*8,800*
Abandonments	18,000	12,000*	12,000*
Net change in active stock	(3,930)	(6,360)*	(3,200)*

** Estimated.*

As the table shows, new construction rates in 1971 and 1972 were actually a little below average rates in the previous 5 years. Net conversions, which had provided a small source of increase in the number of housing units during the latter half of the 1960s, became a source of net decrease. At the same time, the number of demolitions rose substantially. Abandonments are more difficult to estimate. However, it would appear from the workload confronting various problem buildings programs, and from other indirect sources, that abandonments have declined from their 1960s levels but are still averaging at least 12,000 units annually. On this basis, the net decline in the active stock was greater in 1971 than in the preceding 5 years; in 1972, the housing stock continued to shrink, although at a lower rate.

This picture is slightly changed if we examine housing starts, rather than housing completions. Table 7 shows the number of new construction starts for each year since 1966 and compares them to the number of demolitions. The table shows that new starts did increase in 1971 and 1972, although demolitions were correspondingly higher as well. In 1973, however, the number of starts fell back to the 1970 level.

Table 7

Construction – Starts and Demolitions
Thousands of Units

	New Units Started	Units Demolished
1966	20.0	6.9
1967	15.0	6.0
1968	19.8	12.1
1969	14.3	13.2
1970	27.0	10.8
Average 1966-1970	19.2	9.8
1971	29.8	14.8
1972	42.3	13.1
1973	26.0*	NA

** Estimated.*

Little of this recent increase in new construction can be attributed to Vacancy Decontrol and MBR. Table 8 shows that the number of conventionally financed (i.e., private, unsubsidized) housing units fell substantially, while public and publicly assisted housing rose to a record proportion of total new construction (despite uncertainties created by the Federal moratorium on subsidy funds for new housing construction).

Table 8

Sources of New Construction

	Conventionally Financed Units Started		Public and Publicly Assisted Units Started	
	Number	Percentage of Total Starts	Number	Percentage of Total Starts
Average 1966-1970	9,600	48.2	10,320	51.8
1971	7,300	22.6	25,070	77.4
1972	7,900	18.9	33,930	81.1

Section 421 Tax Abatement/Exemption. Much of the increase in the volume of new construction during the past several years can be attributed to Section 421 tax abatement/exemption program. This program had the following major provisions:

1. New buildings with more than 10 units were exempted from the increase in property taxes resulting from their construction. The exemption declines from 100 percent in the first 2 years of occupancy to 80 percent in the next 2 years, 60 percent in the fifth and sixth years, 40 percent in the seventh and eighth years, and 20 percent in the ninth and tenth years.

2. To receive exemptions, buildings had to be on sites which were vacant or underutilized as of October 1, 1971.

3. The rents on initial occupancy had to be 15 percent below rents on comparable newly constructed units in the same area.

The Section 421 program produced 58.4 percent of all buildings of over 10 units constructed between 1971 and 1973. Sixty-two percent of new buildings of this size were constructed in Manhattan, and 21 percent in Queens, with the remainder scattered throughout the other boroughs.

Apart from the question of whether these buildings would have been constructed anyway, without Section 421, there are several major objections to the continuation of this program.

First, it is a program that directly subsidizes upper-income households. Table 9 shows the rent distribution projected for the units built under Section 421, and the income levels required to afford a 2-bedroom unit at a rent-income ratio of 25 percent.

Table 9

Rents of Section 421 Housing

Monthly Rent Per Room	Percentage of Units	Income Levels Required
Under $80	11.1	$15,000
$80-$99	10.1	19,440
$100-$119	19.7	23,760
$120-$139	21.2	28,080
$140 +	37.9	30,240 +

Second, there are serious defects in Section 421's program structure. The amount of the subsidy is based on the assessed valuation of the property; since the assessed value depends on the rent roll, the program gives larger subsidies to higher-rent buildings. Thus, the program is explicitly regressive in its incidence. Moreover, as the exemption is reduced, rents must rise gradually over the first 10 years and then rise sharply when the exemption is withdrawn. This jump in rents will not only confront tenants in occupancy with large rent increases, it will also greatly increase the problem of marketing the apartments. If the buildings are not viable at market rents now, there is no reason to believe that they will become so in 10 years. The City's experience with its Mitchell-Lama program, whose projects have large deficits because tenants cannot meet the rents necessary to keep the projects economic, suggests that the Section 421 program is shortsighted in approach.

Third, the program's criteria for eligibility are very loose - almost any building in the City can qualify. Such a random approach to subsidizing upper-income households seems perverse, especially when the same funds could be used to subsidize low-income households in much greater need of assistance.

The Housing Development Corporation. The Housing Development Corporation (HDC) has so far provided mortgage financing for about 6,000 middle-income units. Since the HDC program is self-financing, it provides a highly desirable means of increasing the availability of housing for middle-income tenants, and should be continued. However, the utility of its program for low-income tenants will be dependent primarily on the direction of Federal housing policy in the future - especially whether Section 236 and rent supplement subsidies will continue to be provided.

In summary, the City's efforts to stimulate new construction have been poorly structured and largely ineffective. The primary emphasis has been on upper- and middle-income housing, and very little of the new construction has been directed at the income levels most in need. This would not be critical were it not for the fact that the existing housing stock - at least at the low-rent, low-quality range - continues to be short of funds, as do the City's various programs aimed at improving the quality of this portion of the stock. Some redirection of the City's financial assistance is clearly desirable.

Municipal Loan and J51. The City has substantially expanded its rehabilitation efforts. Funding for the Municipal Loan program has been raised to $70 million for the 1973-1974 fiscal year and the utilization of the J51 tax abatement/exemption program, covering major capital improvements, has been increased. Despite these steps, the volume of rehabilitation starts achieved was only 1,904 units in 1971, and 1,980 units in 1972 - down from an average of 2,300 units between 1966 and 1970.

The Municipal Loan program continued to be targeted at core areas and emphasize gut rehabilitation - in 1972-1973, the average loan per unit was $22,400. Under the J51 program, 1,546 buildings were assisted in 1972-1973, of which 237 had major capital improvements. The value subject to abatement was $10.5 million, and subject to exemption was $132.3 million (thus costing the City about $8 million in forgone property tax revenues). But the structure of this program continued to be deficient because of poor criteria for determining need for assistance, and overcompensation of expenditures.

Rehabilitation Mortgage Insurance Corporation. The process of neighborhood preservation requires large amounts of capital. Given the limitations on public funds, it is essential that the public sector leverage itself by attracting complementary private capital. In order to facilitate this process, the Rehabilitation Mortgage Insurance Corporation (REMIC) was established in 1973 to insure private rehabilitation loans, and by reducing

their riskiness, encourage investment in deteriorating areas. REMIC was authorized to insure one-third of rehabilitation loans made, and up to 20 percent of preservation loans (loans which enable building acquisition or recasting of maturing loans). Financial institutions which agreed to participate in the program in a neighborhood preservation area were required to offer preservation loans to its existing mortgagors in the area, in order to ensure a continuing source of mortgage capital.

The authorized capital of REMIC was initially set at $7.5 million; the corporation could insure loans of 20 times this amount: $150 million. This compares with a total rehabilitation requirement of approximately $7.5 billion in the City. REMIC's insurance program could also be used in conjunction with Federal and City rehabilitation loan programs, and additional financial instruments such as joint City and private participatory mortgages, to multiply the impact of its own limited appropriations and powers.

* * *

Over the past 3 years, 29 percent of the controlled housing stock has been decontrolled. Rents have risen by about 46 percent under the combined impact of the Vacancy Decontrol and MBR programs, thus increasing the severity of the problems confronting low-income tenants. Seventy-three percent of the rent gap has been filled so far, and if the MBR and Vacancy Decontrol programs continue without modification, the rent gap will be fully closed by mid-1975, and landlords will thereafter be overcompensated. Thus, the first issue confronting policy makers is how to strike a more appropriate balance between the financial needs of the housing stock and the financial needs of low-income tenants.

These rent increases have not materially improved the quality of services from the existing housing stock. The City's effort to improve code enforcement has simply bogged down the MBR program itself; its other problem buildings programs are still constrained by limited funds and, in several cases, poor program structures. Meanwhile, the City has continued to subsidize new construction for middle- and upper-income households; yet the rate of new construction has not risen sufficiently to offset losses from the existing housing stock. A renewed and even strengthened policy emphasis on the existing housing stock is needed, backed up by sufficient funds and personnel.

3- Proposals for Change

In this chapter, we present specific recommendations for changes in City housing policies and programs. These recommendations are predicated on a number of basic principles which we think should govern City housing policy - and State policy insofar as this provides the framework for City actions - over the next few years. Accordingly, we first outline these basic principles and then proceed to discuss our specific recommendations for programmatic change.

PRINCIPLES OF REFORM

We believe that the following basic principles should govern housing policy in New York City:

1. The primary focus of City housing assistance should be on lower-middle-income households. These are households who do not receive any significant public assistance in the form of welfare or social security, but have incomes which are too low to afford them access to decent housing at market rent levels. Generally, 4-person households included in this group would have incomes between $4,000 and $12,000; the income levels for larger households would be somewhat higher. The City should not continue programs whose primary beneficiaries are upper- and middle-income households. Households with incomes lower than these levels require broad financial assistance, rather than specific housing assistance; and this must be provided primarily by the Federal Government.

2. The City should emphasize the maintenance of the existing housing stock, rather than new construction. Subsidizing new construction for higher income levels is a wasteful use of public funds for the benefit of those who least need assistance. Subsidizing new construction for low-income or lower-middle-income households is inefficient: it requires large per-unit subsidies, reduces the number of low-income or lower-middle households which can be assisted, and provides benefits to those lucky few able to get

access to the new housing while excluding from these benefits others at the same income level.

3. Within the existing housing stock, rents should reflect an appropriate balance between the financial needs of owners and tenants' ability to pay. Thus, landlords should not be asked to subsidize their tenants; on the other hand, tenants should not be asked to bear disproportionate expenditures to dwell in decent housing. Government should adopt the financial obligation to fill the gap between what tenants can reasonably afford to pay and the rents required to adequately preserve and maintain the housing stock.

4. Rents should continue to be regulated to give owners a reasonable return while preventing exorbitant rent increases. A total reliance on the free housing market would result in major social and economic dislocations within the City.

5. Any system of rent control should be simple to administer and easily understood by both landlords and tenants. The City's capacity to administer complex programs requiring millions of case-by-case decisions is, and will continue to be, very limited. Future regulatory systems should stress simplicity in design and implementation. While fiscal and administrative controls over City programs should certainly be strengthened, the programs themselves should be simplified and made, to the extent possible, self-enforcing.

6. The City's involvement in apartment-by-apartment decisions should be minimized. To the extent possible, the City should create housing market conditions in which increasing reliance can be placed on direct negotiations between landlords and tenants. This will require strengthening landlords' and tenants' legal obligations to each other, as well as both groups' legal rights and remedies. In particular, inequities in powers of enforcement inherent in current landlord-tenant law will need remedial action. These legal changes - as well as the design principles of a new rent regulation system -, can create the conditions necessary for policing by landlords and tenants of rent collection and the provision of housing services.

Acceptance of these principles would require substantial modification of the City's current housing programs. In the following sections, we

briefly discuss the major program changes which appear to us to be desirable.

REFORM RENT CONTROL

The most urgent issue confronting policy makers is whether the Vacancy Decontrol and MBR programs should be reformed, and if so, what system of rent determination should take their place. We recommend that:

1. The Vacancy Decontrol law be repealed by the State Legislature

2. The current MBR system be substantially modified, primarily to simplify the program structure and make it both comprehensible to landlords and tenants and more easily administered by the City

3. A new, simple, uniform system of rent regulation be adopted for the entire existing rental housing inventory, including buildings which are currently under Rent Stabilization and Rent Control, as well as buildings which have been decontrolled under the existing Vacancy Decontrol law.

4. The new rent control system has four central features:

    a. Vacancies should no longer form the basis for rent increases, whether to market levels (Vacancy Decontrol) or MBR levels (MBR program)

    b. MBRs should be calculated for each building, but not for each apartment, thus eliminating a large proportion of the data requirements and clerical work necessary under the current MBR program

    c. Rent increases should be uniform for all apartments, and should be based on an index of aggregate personal income in the City; thus rents should increase only as tenants' ability to pay these rents increases

    d. The City should institute a program of financial assistance which, on a building-by-building basis, would make up the gap between the aggregate rent roll and the aggregate MBR.

Below, we provide the rationale for these recommendations and explain how the new system of rent regulation would work.

Repeal Vacancy Decontrol

The arguments for repealing Vacancy Decontrol are straightforward. First, Vacancy Decontrol has led to very substantial rent increases. These increases were necessary to close the rent gap, but this purpose will have been essentially accomplished by mid-1975 (or even earlier), and thereafter a continuation of Vacancy Decontrol will overcompensate landlords, enabling them to more than recover their costs and earn a more than fair rate of return. (See Exhibit XXIV.) The impact of these increases on tenants could theoretically be mitigated through some form of rent assistance; but it does not appear likely that a rent assistance program will receive serious consideration at this time (for reasons of both cost and administrative complexity). Moreover, even with rent assistance, some form of rent regulation would be needed, because there is no justification for assisting tenants to pay rents above those required to provide a fair return to building owners. Without a rent assistance program, the need to regulate rents is correspondingly greater - in order to ensure rent levels that are fair to both landlord and tenant.

Second, Vacancy Decontrol (and, to a more limited extent, Rent Stabilization) has created serious inequities among tenants at the same income level - with some tenants being forced to pay much higher rents, and consequently much higher proportions of their incomes, than other tenants at the same income levels.

Third, any system which grants major rewards to vacancies is bound to create incentives for landlords to harass tenants or otherwise pressure them into leaving. The evidence presented in Chapter 2 - that over 330,000 complaints were filed by tenants in 1972 to protest decreased services - partially corroborates this conclusion. In addition, 2,500 complaints of direct harassment were received, and 1,700 landlord attempts to evict their tenants were denied by HDA. A continuation of Vacancy Decontrol would prolong the invitation to harassment and other unpleasant effects on a large proportion of tenants. This program should be replaced by a system that neither rewards nor penalizes vacancies.

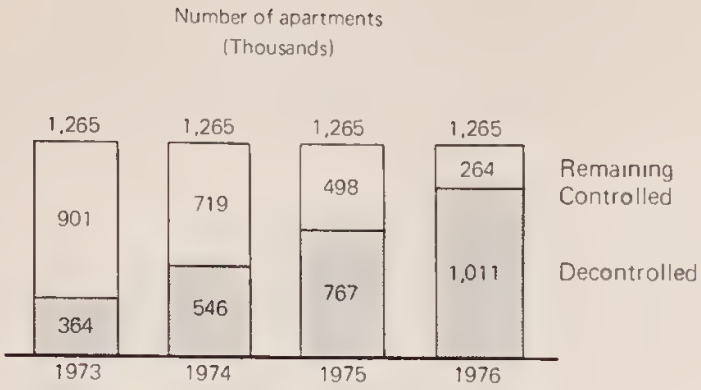
Vacancy Decontrol was originally intended to dismantle an overly rigid and politicized system of rent control. However, a new system of rent regulation - simple, fair, and easily administered - could achieve these objectives equally well, and Vacancy Decontrol need not be continued for this purpose.

Should repeal of Vacancy Decontrol be accompanied by a rollback of rents? An argument could be made for rollback, primarily on the grounds

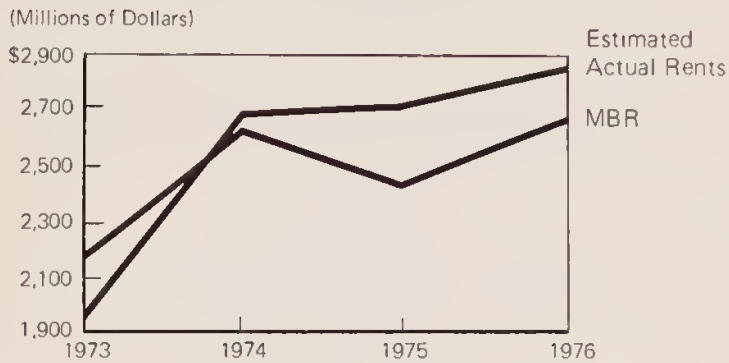
Exhibit XXIV

Continuation of vacancy decontrol would lead to high rates of return . . . .

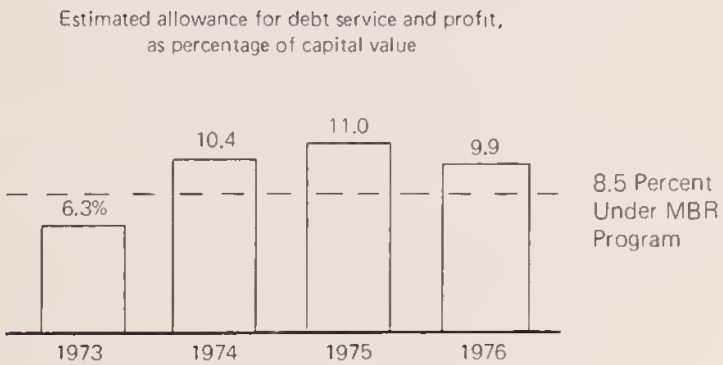
The number of decontrolled apartments would rise rapidly . . . .



Rents would rise above MBR levels . . . .



And return on equalized assessed values would rise . . . .



of restoring equity among tenants. Rents could be rolled back either to predecontrol levels or to the appropriate MBR levels. If rents were rolled back to predecontrol levels, equity would not be achieved, because tenants in formerly decontrolled apartments would then be paying lower rents than tenants whose apartments are under the MBR program. On the other hand, rollback to MBR levels would create massive administrative problems. Computation of MBRs for decontrolled apartments would require the following steps:

1. All decontrolled apartments would have to be identified as such. Since there is evidence that decontrol notifications have not been filed for many apartments, this would be a major task in itself (each tenant's claim that the apartment he or she occupied was decontrolled would need to be verified).

2. The data required to compute the MBR for these apartments would have to be verified - especially the number of rooms in the apartment.

3. The eligibility for MBR would have to be cross-checked - by identifying the building in which the decontrolled apartment was located, and checking its code violation and essential services status.

4. Rent orders would have to be issued for each apartment - to both landlord and tenant - and inevitably a large number of landlord and tenant complaints would have to be dealt with.

An effort of this magnitude would constitute another major crisis for the City's Department of Rent and Housing Maintenance - and would needlessly create further difficulties for both landlords and tenants. A simpler, more easily attainable goal should be established: to ensure that tenants now in decontrolled apartments do not suffer further worsening of their situations by being confronted with further rent increases on lease renewal. The existing rental base should be accepted and should serve as the starting point for new rent regulation policy.

Modify the MBR Program

The MBR program was a rational response to the severe problem of improving equity among building owners and tenant groups. It provided a relatively objective method of calculating ceiling rents to yield a fair return to owners without enabling unrestrained rent increases to whatever level

the market would bear, and of reducing the disparity of rents for similar apartments.

However, the MBR system achieved these objectives at the expense of an almost insurmountable administrative problem. Basically, the system required the following major sets of activities in order to implement rent increases:

1. Submission of landlord data (including total number of apartments and rooms in the building, the size of each individual apartment, the amount of commercial space, the rent for this commercial space, and many other items), verification of these data by the City, and establishment of procedures to handle claims by tenants that landlord-submitted data were incorrect

2. Collection of other data from City sources - such as the assessed valuation of the property, the real estate taxes paid, water and sewer charges, and the amount of tax abatement and exemption

3. Mailing out of requests for landlord certifications that essential services were being maintained and that the housing was substantially free of code violations; processing of these certifications; and identification of buildings ineligible for MBR increases

4. Computation of MBR building rents, and allocation of these to individual apartments

5. Issuance of rent increase orders to individual tenants, and to landlords

6. Processing of thousands of complaints about false certifications or inaccurate data.

The essential objective of the MBR system can be achieved, while eliminating a large proportion of the administrative work load implicit in the system, through some fundamental modifications to the program.

First, the calculation of individual apartment rents should be eliminated. The need to calculate rents for each apartment greatly increases the data required and the problems of verification. It requires the mailing out of rent orders to each occupied apartment; tenant misunderstandings create a tremendous confusion and a further workload in responding to inquiries and tenant complaints. Meanwhile, the advantages to be gained from the

calculation of individual apartment MBRs are rather small - in 1974, about 80 percent of all apartments will receive increases of between 6.0 and 7.5 percent. Given the uniformity of rent increases, a simpler system of determining the apartment-by-apartment increase could be instituted.

Second, a new system of determining rent increases, linked to increases in disposable income, should be implemented. This system should have two essential features. First, it should be very simple and easily understood by tenants: most preferred would be a system which provides the same percentage rent increase to all apartments. If the City were to announce each year a single rate of rent increase, all tenants would know immediately what their new rents were, and would not require resort to a City bureaucracy to determine whether they were paying the legally collectible rent. This would, at a stroke, very substantially diminish landlord-tenant contention as to the "correct" level of apartment rents, and would also diminish the City's involvement in verifying and cross-checking these rent levels.

The new system should also bear some relationship to tenant ability to pay. This suggests that the percentage increase in rents should be linked to the increase in disposable personal income in the City. The City would, each year, calculate the percentage amount by which disposable income had increased in the prior year; this percentage figure would become the increase in rent levels allowed in the current year.

This system would not perfectly achieve any of the more sophisticated goals of housing policy - such as equalizing rent-income ratios, eliminating rent skews, and finely calibrating the amount of assistance to each tenant according to his income. But it would broadly meet the goals of equity - dollar increases for higher-rent apartments (predominantly occupied by higher-income tenants) would be larger than for lower-rent apartments; and rent-income ratios would not worsen unless drastic increases or decreases in individual incomes took place. Substantial equity and protection of tenant incomes would be achieved, without requiring concerted bureaucratic action by the City. In practice, this simpler system might achieve greater equity than a more complex, but administratively infeasible, system.

Third, building-wide MBRs should continue to be calculated. The purpose of these calculations would be to provide a standard against which to measure the rent roll of a building. Limiting rent increases on a simple index basis, as suggested above, might ultimately result in the reemergence of a City-wide rent gap, or might substantially raise rents above MBR levels.

In order to determine whether current rent levels were adequate, the Department of Rent and Housing Maintenance would:

1. Collect data on current rents (these data are already available for most apartments)

2. Compute the total actual rent roll for the building

3. Compute the MBR for the building

4. Determine the difference between the actual rent roll and the MBR rent roll.

Each year, when the City-wide rent increase percentage was announced, the following steps would be taken:

1. The Department of Rent and Housing Maintenance would calculate the new rent roll for the building (a trivial computation)

2. Buildings whose rents were below the MBR would receive the average City-wide rent increase, or the increase required to reach MBR levels, whichever was less

3. Buildings whose rent rolls were above the MBR would receive no rent increases

4. Buildings whose rent rolls were below MBR even after the rent increase would be identified for financial assistance.

In order to eliminate any confusion, the current building rent roll, the building MBR and the percentage difference between these two figures, would be posted visibly in the building on (say) March 1 of each year. The rent increase percentage would be announced on (say) June 1 of that year. It would be a simple matter for tenants to check whether they had to pay the full increase, a partial increase, or no increase, by comparing this City-wide average increase to the posted difference between MBR and the current building rent roll. The system would be straightforward and self-enforcing.

Exceptional rent increase provisions - such as those for major capital improvements - would continue to operate. The building rent roll would simply be adjusted to take these into account.

However, no rent increases would be given on vacancy. This would make the landlord neutral between retaining the current tenant or getting a

new one, and would thus remove the incentives to harassment provided by both MBR and Vacancy Decontrol. On the other hand, it would in no manner restrict the landlords' right to evict tenants for nonpayment of rent, vandalism or other due cause. Normal rent losses from apartment turnover would continue to be compensated under the vacancy and collection loss component of the MBR formula.

Fourth, a single uniform system of rent regulation should be applied to the entire multiple-dwelling rental housing inventory. Simplicity is of enormous importance to tenant rights. A surprisingly large number of tenants do not currently know or understand their control status, and obviously are in no position to enforce the rights or legal remedies they theoretically have under each control or stabilization program. With a single system, whose rules were clearly articulated and understood, tenants' powers to police rent collection would be greatly strengthened, and the bureaucracy's role in performing this function could be correspondingly reduced.

Fifth, the City should incur the obligation to provide the difference between actual rents and the MBR for those buildings still below MBR. The number of such buildings would be relatively small, since the difference would be calculated on a building-by-building and not apartment-by-apartment basis (i.e., excess rents on apartments above MBR would offset rent deficits on apartments below MBR). The subsidy could probably best be provided through tax abatement, since this is legally and administratively the simplest implementation vehicle.

In the absence of building-by-building data, we can provide only an indirect estimate of the potential cost of this program. On the aggregate, the rent gap, calculated using the current MBR formula for 1974, is about $400 million in January 1974. 1974 rent increases under the MBR program will reduce this to $320 million, and an appropriate change in the MBR formula itself (to provide a more reasonable return on capital value) would reduce it to about $103 million. If the new rent regulation system were adopted in July 1974, Vacancy Decontrol would have nearly eliminated the overall rent gap. However, some low-rent buildings with predominantly low-income tenants would still be below MBR rent levels; this deficit would probably be in the neighborhood of $25 million to $35 million. Accordingly, the first-year cost of the program would certainly be under $50 million.

Costs in subsequent years would depend on the relative rates of increase in incomes and the operating costs of housing. Based on historical trends, MBRs would rise about 5 percent per year, and disposable incomes (hence

collectible rents) would rise about 4.5 percent annually. The difference would amount to about $20 million to $25 million per year and this would be an incremental subsidy cost. This cost would, of course, be reduced by any increase in the level of Federal assistance, or any other favorable changes in the City's economic situation which would raise the City's aggregate personal income. To put these costs in perspective, they amount to less than 1 percent of the City's operating budget, and to less than 4 percent of its real estate tax yield.

Sixth, the rent increase index should be calculated by an independent impartial group outside the City administration. The technical work might best be done by an agency like the Census Bureau; the work would be overseen by a Rent Regulation Board with representation from the State government, City agencies, and landlords and tenant groups. The purpose would be to ensure that the rent determination process was viewed as being impartial, and not subject to political manipulation.

Finally, the linkage of the MBR system to code enforcement should be reformulated. The need to precertify code violation status has greatly increased the paper work necessary to implement MBRs, without having any perceptible effect on housing quality. The code enforcement effort should be strengthened and expanded; cutting its artificial linkage to MBR would allow the program to respond to its own operational logic, rather than to arbitrary criteria related to meeting MBR system requirements.

In summary, then, the proposed rent regulation system would have several advantages: It would be simple to administer, would strengthen direct landlord-tenant enforcement, relieve the City's bureaucracy of considerable processing workload, and enable the City to reduce its participation in apartment-by-apartment decision making. Above all, it would prevent any further worsening of rent burdens on tenants without penalizing landlords. The rapid rent increases under MBR and Vacancy Decontrol make the program feasible at relatively small cost to the City and State governments - and this cost would be well worth the improvement in landlord-tenant relationships and other benefits that the program would have.

Revisions to rent control should be supplemented by several other programmatic and legal changes. These are discussed in the following sections.

REVISE PROGRAMS TO IMPROVE HOUSING MAINTENANCE

In addition to the rent control reform proposed in the preceding section, the City should undertake a number of revisions to its programs that are directed toward improving the quality of housing currently occupied by City residents. Three basic principles should govern these efforts:

1. State and City resources for housing assistance or subsidy should be reallocated away from new construction and major rehabilitation toward programs which emphasize improvements in the quality of existing housing. New construction and major rehabilitation are expensive and, due to high costs, primarily benefit upper-income tenants. With very high per-unit capital costs and limited public funds, City efforts to directly finance new construction and major rehabilitation can produce only an extremely limited number of units. These same funds could be better deployed in a variety of assistance and enforcement programs aimed at stemming deterioration of the existing housing stock.

2. With increased resources, the City's casework programs, including Code Enforcement and a variety of other problem buildings programs, should be improved in terms of their targeting and operational procedures. In particular, the programs should be more narrowly focused on segments of the existing housing stock which will most likely respond to treatment.

3. With most of the deficit in rental revenues now eliminated, the burden of ensuring adequate maintenance and enforcing a minimum level of housing services should be shifted from the City to tenants. Strengthened legal rights for tenants would better enable them to negotiate directly with landlords, reduce their reliance on the City's bureaucracy to enforce their rights, and accordingly enable the City's programs to be more coherently programmed rather than reactive and complaint-oriented.

These three mutually supportive changes would go a long way toward improving the quality of occupied housing in the City. Legislative and programmatic steps required to implement these changes are discussed briefly in the following sections.

Reform Landlord-Tenant Law

In those portions of the rental housing stock where building revenues are now adequate to support proper building maintenance, the primary burden of ensuring adequate delivery of housing services should rest on tenants. This is impossible under the antiquated legal remedies available to tenants under current law; the law should be revised by the State Legislature to clarify landlords' and tenants' legal obligations to each other, and to strengthen tenants' abilities to enforce their rights through the medium of the Housing Court.

Under current law, tenants' rights are heavily restricted, in the following ways:

- ¶ Tenants are compelled to sign away most of their rights to legal recourse against the landlord, when they sign their lease

- ¶ Tenants have no legal recourse when needed apartment repairs are not made; they must wait until a household member is injured before commencing proceedings against the landlord

- ¶ Where a "health impairing" violation exists, the tenant may withhold rent; but only the landlord can begin legal proceedings, and the tenant must deposit accrued rent with the court until a decision is arrived at

- ¶ In most circumstances, the tenant must continue to pay rents despite inadequate maintenance or provision of services.

The result of these deficiencies in tenants' abilities to assert their own rights has been increasing reliance on the City to enforce the tenants' right to a habitable dwelling unit. This has theoretically required the City to respond to all tenant complaints, to inspect all housing units periodically, to undertake necessary negotiations with landlords, and to invoke legal penalties and compulsion where necessary. In practice, the City has proved inadequate to this gigantic task, and the workload has swamped even those City programs which could adequately respond to more limited objectives.

Accordingly, the following provisions should be legislated:

1. Lease agreements should include a specific statement that the landlord is obligated to comply with housing codes, to make

repairs necessary to ensure that housing is fit for occupancy, and to maintain essential services.

2. Lease provisions which limit tenants' rights to counterclaim in court action, or which arbitrarily limit landlord liability, should be prohibited.

3. Tenants should specifically be vested with the right to sue for injunctive relief, to compel restoration of housing services, and to take legal action to ensure compliance with housing codes. In particular, tenants should be vested with the right to bring actions to the Housing Court.

4. Landlords should be required to pay tenants' security deposits into a special account, to be used for necessary repairs in the event of an owner's refusal or inability to undertake repairs. This account would then be replenished by escrowal of monthly rent payments.

Implementation of these provisions would greatly reduce the current overload on the Office of Code Enforcement, and would enable the Code Enforcement program to be better targeted and more properly focused on those segments of the housing stock most in need of inspection and treatment.

Reorient Code Enforcement

The Code Enforcement program should be strengthened, and should become part of a more comprehensive housing inventory management strategy. The elements of such a strategy would include improved coordination of rehabilitation, problem buildings, and Code Enforcement programs; targeting of these programs to the limited number of buildings in the City which have a high proportion of all code violations, are in need of case-by-case attention, and are not so deteriorated that they are unsalvageable. In order to achieve this, the following steps should be taken:

1. Closer coordination should be established between the Office of Housing Rehabilitation (currently in the Department of Development), and the Department of Rent and Housing Maintenance. Serious consideration should be given to merging these two entities, especially if the coordinative superstructure of HDA is to be dismantled.

2. Resources allocated to the construction of a building-by-building data base should be substantially expanded. A current, comprehensive data base is a prime necessity for the coordination of the City's various problem buildings programs, and also for the operational streamlining of the Code Enforcement program itself. In order to reduce duplicate inspections of the same building, repeated inspections for the same violations, repeated contacts with the same landlord, and other inefficiencies that waste inspectional time, it is necessary that local code enforcement offices be able to check tenant complaints against a data base which shows what the building's violation status is, whether it has recently been inspected, and what action has already been taken - for example, whether the building is already in a treatment program. This data base would also be used to determine the appropriateness of alternative forms of treatment, assistance, and compulsion, as well as to track physical and financial indicators of building condition that are useful in anticipating the likelihood of abandonment.

3. With this data base in place, local code enforcement offices should be linked by computer terminal to the central file and should be able to update this file on a current basis.

Refocus Rehabilitation Programs

The City's rehabilitation programs should be substantially modified. The programs should be oriented away from gut rehabilitation in core areas toward moderate rehabilitation in the context of a concerted effort to preserve deteriorating but salvageable neighborhoods. Gut rehabilitation should be limited to those instances in which buildings are about to be transferred to cooperative tenant ownership, and the tenants can fully afford the higher postrehabilitation rentals which will result. Minimum and moderate rehabilitation should be emphasized.

In addition, the City should accelerate its efforts to reduce its own role as direct lender of rehabilitation funds. Major steps in this direction have been taken with the authorization of the Housing Development Corporation to lend $200 million for rehabilitation, and with the establishment of REMIC's mortgage insurance program. However, the City should consider going further, by developing secondary mortgage market operations similar to those developed by the Federal Government for new construction. These might involve the transference of City loans to local banks and other financial institutions, the use of "pass-through" mortgages as a means of raising private capital for rehabilitation, and other similar techniques.

In addition, the City should consider the possibility of encouraging local rehabilitation and housing maintenance organizations. Currently, the inexperience of many owners of small buildings in determining the physical requirements for their buildings, in negotiating with rehabilitation contractors, and in managing and controlling the costs of rehabilitation work undertaken is a major contributor both to the low level of rehabilitation and its high costs. The City could encourage the development of a local rehabilitation and maintenance "industry," by providing both financial and technical assistance and establishing local, community-based corporations to undertake this work. In addition, these corporations might be used as "managing agencies," undertaking to maintain and manage buildings for a fee.

The City's role would be to establish these corporations, or to appoint existing management agencies as contractors for given geographical areas, and to participate in negotiating terms for landlord and managing agent satisfactory to both. This "centralization" of rehabilitation and maintenance skills, together with geographic concentration of these rehabilitation-maintenance corporations, could substantially improve the efficiency and lower the costs of building maintenance and repair.

Expand Ownership Change Program

While Code Enforcement, moderate rehabilitation, and other treatment programs should all be strengthened, in some areas of the City, abandonments will continue due to basic rental revenue deficiencies or landlord-tenant hostility. In these areas, the transfer of building ownership to low-income cooperatives offers the best hope for reducing the rate of losses from the housing stock. Home ownership - and the dignity of possession - can become a key element in preventing housing decay. Tenant-induced housing deterioration can be reduced; tenant cooperation in maintaining the building can be harnessed; and tenant participation in rehabilitation can substantially reduce rehabilitation costs. The reality of these expectations is borne out by the success of the City's small ownership change program initiated in 1973. This program should be substantially expanded. Accordingly, the State and City should:

1. Strengthen the mechanisms to take into receivership at least those buildings which the owners voluntarily wish to relinquish. The owner should be able to call the City and transfer ownership within 2 or 3 months.

2. Simplify processing, enabling a speedier transference of title to the tenants.

3. Institute major tenant education and training programs, which should accompany transference of title to the tenants. These programs should be run on a continuing basis by HDA and should emphasize the essentials of management, maintenance, and repair.

4. Encourage tenant-owners to contract with the special rehabilitation-maintenance corporations described in the previous section.

* * *

Increased emphasis on maintenance and renovation of existing housing, together with legal changes to strengthen tenant participation in maintenance and management of the stock, are essential to improving the quality of housing enjoyed by the majority of City residents.

DE-EMPHASIZE NEW CONSTRUCTION

The City's latitude with respect to new construction is limited. Huge resources would be required to meaningfully raise the rate of new construction. Moreover, these resources could be better used in improving the existing housing stock.

However, the City can take some limited steps to encourage greater private participation in new construction. Two major opportunities seem to exist: zoning revisions and the institution of mortgage insurance programs for new construction.

Revise Zoning Law

The change in the zoning law which took effect in 1965 adversely affected new construction, by reducing allowable residential density and, therefore, raising per-unit land acquisition and development costs. The new administration should undertake an intensive study to determine how - at least in limited areas of the City - these restrictions can be relaxed. Some areas of the City could clearly support higher residential densities and might once again become attractive for new construction if per-unit costs could be reduced. While this would mostly be upper-income housing, making

construction of such housing once again economically feasible would at least eliminate the necessity for subsidization of upper-income households through such programs as the Section 421 tax abatement/exemption program.

Provide Mortgage Insurance

The other step which the City should consider is the extension of the REMIC concept to new construction. A mortgage insurance program, funded and administered by the City, might help stimulate new construction by reducing the risks associated with mortgage lending in central City areas. Such a program would complement existing mortgage lending activities, and might ultimately reduce the burden on the City's debt limit by providing security other than the City's taxing power for bonds used to finance the mortgage loans.

Eliminate Subsidy Programs

While taking these steps to encourage private new construction, the City should begin to limit its own subsidization of new construction activities in order to release funds for programs aimed at the existing housing stock. The Section 421 tax-abatement/exemption program should not be extended beyond its current life, and the City should consider a major refocusing of its Mitchell-Lama new construction program. This has increasingly been oriented toward higher-income groups or has suffered from rental deficits and high rates of default on mortgage loans, where existing tenants have been unable to afford the increases in rents necessary to keep up with rising costs of operation.

CHANGE REAL ESTATE TAXATION

Finally, two changes in real estate taxation should be undertaken:

1. In order to reduce the costs of rental housing, the real estate tax component of rent should be separated and should be levied directly on the tenant, instead of on the owner as at present. This would make this component of rent deductible from the Federal income tax paid by the tenant, and would effectively reduce rents by amounts varying from 4 to 10 percent, depending on tenant income level. The building owner would continue to collect the taxes with

the monthly rent payment, and remit them to the City. No more than a simple legal change is required; the feasibility of this proposal has now been established beyond question.

2. In order to encourage new construction, the City should reexamine real property assessment practices to determine how assessments on underutilized sites can be revised. Current assessment procedures discourage development by taxing developed properties more heavily than underdeveloped properties. A revision of these incentives - especially in a highly inflationary situation in which large profits can be made from holding land for resale - is necessary in order to encourage the construction of new housing.

* * *

None of the individual proposals outlined in this paper is dramatic. However, together they add up to substantial changes in emphasis of housing policy and would require some reallocation of public resources devoted to housing. We believe that the adoption of these proposals would represent important steps in the direction of better housing for the people of New York City.

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Frank S. Kristof
Director
Division of Economics and Housing Finance

M E M O R A N D U M

TO: Carter F. Bales February 21, 1974

FROM: Frank S. Kristof

SUBJ: Comments on: A Housing Agenda for New York City

The analytical work in laying the groundwork for the ultimate recommendations is sound. I find minor discrepancies and errors at points but this is inevitable unless one has been immersed in local housing customs and lore for a good part of his life. For example, Section 421 of the Real Property Tax Law is a tax exemption program, it is not tax abatement/exemption. Second, in your Table 8, I think you have the Section 421 starts under publicly-assisted housing which technically is correct but since this is only a 10-year tax exemption program and the housing is privately-financed, it is my judgment that these starts should be credited to the private sector. Rents that are within the range of $110 to $125 certainly is a conventional housing price class (as are those of some of our M-L's).

There appear to be some contradictions in the data shown in Exhibit 11 and the discussion about municipal loan on page 54. The rehabilitation figures are not consistent. In Exhibit 22 (page 41) and Table 3 (page 42) the amount you attribute to vacancy decontrol is erroneous. You must be aware that at least 40 percent of the amount attributable to vacancy decontrol would have occurred anyway under MBR. I think this conceptual distinction must be made in a proper analysis of the effects of vacancy decontrol.

The foregoing are the only factual observations I would make for the first two chapters of the book. Substantively, I agree with your objection to tax exemption for high income families. It is a further distoration of existing inequities in New York City's housing subsidy system. You and I were at one on this subject eight years ago. Only one possible excuse might exist for this type of exemption --as a production incentive system to produce housing that otherwise would not be produced. There is a real possibility that many of the sites that have been developed under

Section 421 might have been pushed upon the City and State housing agencies ultimately as M-L's with 40-year 10 percent of shelter rent tax exemption.

Given the Ruppert Brewery, Waterside and Welfare Island examples, and the new 42nd Street project being developed by the City which surely will come out at $120 per room per month (rather than the advertised $103 per room) one may raise a question whether it is better to produce these units with limited tax exemption than not having them produced at all or, if they are produced, to find them created with deep tax subsidies. This is a rationalization but we are dealing with housing decisions that are made politically and not logically.

Chapter 3 - Proposals for Change

I am heartily in accord with points 1,2 and 3. The point 4 thesis that rents should be regulated to give owners a reasonable rent while preventing exorbitant increases is a social concept (like "just price") that does not deal realistically with the production incentive problem in a (relatively) free price system. The distinction between free market prices and exorbitant rent increases is not substantive but rhetoric. For example, when a prospective tenant, who knows nothing about the previous history of an apartment's rent, is faced with an asking market rent for the apartment he makes a decision on the basis of whether he feels the rent is reasonable. He does have freedom to accept the rent, to bargain over it, or to reject it and look elsewhere. I would further challenge anyone to distinguish the difference in value, or reasonableness, between the rent of an apartment moving from a $275 controlled rent to $300 and an identical apartment in the same building moving from $125 to $300. The first apartment was subject to many turnovers, the second was in the same family's hands for 25 years. It is my contention, that in a single turnover, adversely affecting no occupant family, that this apartment has been restored to its market price so long as there are families able and willing to pay this price. I find no rational grounds for an objection to large rent increases for apartments whose rents have been unfairly and inequitably depressed for 25 years because of the anomalies of the rent law.

A major objection that everyone has to the present chaotic rent structure in New York City is the wide disparity among rents of identical apartments in the same building. This creates inequities and hostilities among tenants. Nothing in your proposals deals with these inequities. Straight across-the-board percentage increases within the building perpetuates the existing chaotic rent structure. Vacancy decontrol, or even vacancies under the MBR system, tends to eliminate these differences. In Table 1, I show a random sample of decontrolled rents for 3-room apartments in Manhattan and Brooklyn. I invite you to examine these numbers and show how vacancy decontrol has eliminated the element of choice among families of different income levels except for the lowest-income families ($5,000-$7,000) just above welfare status. I am totally in sympathy with a system for dealing with the rental problems of such families.

I think a system of rent subsidies, whether at the city, state or federal level, for such families would not be terribly costly--averaging perhaps $50 a month to deal with the differences between previously controlled and now decontrolled rents. This would take off the pressure of the worst inequities created by vacancy decontrol. There are perhaps 300,000 such families and probably only 100,000 have been affected to date--which would mean starting with a rental assistance program of $60 million annually and reaching a peak of $180 million some years away. This is less than one third of current welfare housing annual assistance. People within the range of welfare assistance properly should be supported by this type of assistance. This burden does not belong on the property owners' back through artifically controlled rents.

Your analysis already reflects a New York City syndrome relative to rents. I suggest that you should be shifted for a spell to Chicago, San Francisco, Cleveland or Milwaukee where rent control is unknown. The concept of exorbitant rent increases, of "reasonable" compensation to landlords, is a New York City rent control concept. I take you right back to the original Rand argument in 1968 (Rental Housing, Volume II), where they pointed out that the great majority of families in New York City could absorb most if not all the rent increases between controlled and market rents. The section of the population that cannot absorb these increases should receive support from the public sector.

There is nothing unique in New York City's housing market relative to Chicago or San Francisco. Both these latter cities have a high portion of renter population--yet they seem to have survived with a free market rent system. In both the U.S. as well as England's private sector, the only thing rent control seem to have accomplished is to increase the rate of deterioration of existing housing and depress the level of services to absolute minimum levels that owners can get away with. I do not subscribe to such a system and though your proposals are a partial step toward the way of providing equity to existing property owners, they are fatally defective in terms of maintaining a healthy existing rental housing inventory over the long term.

FSK/is

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M E M O R A N D U M

TO: The Files March 1, 1974

FROM: Frank S. Kristof

SUBJ: Supplementary Comments on a Housing Agenda for New York City by Carter F. Bales and A. Puri

In outlining principles of reform, the McKinsey report points out (page 56) that "the City should emphasize the maintenance of the existing stock rather than new construction" and that "within the existing housing stock, rents should reflect an appropriate balance between the financial needs of owners and tenants' ability to pay." The examination that follows suggests that the recommendations of this report in substantial measure fail to support these principles.

In my report on rent control (p. 3) I pointed out that the supplementary income attributable to vacancy decontrol provided $73 million of the $445 million reduction in the gap in the $807 million calculated by Rand in 1968 between market and collected rents. This $73 million has been the margin that has moved a large part of the housing inventory under rent control toward a break-even or profitability point that could never be achieved under any other system without disruptive impact upon occupant tenants.1/

No single fact more dramatically demonstrates this point than the following report from a local financial institution on the effect of fuel oil costs alone:

"This winter's sudden rise in the price of heavy heating oil has cut deeply into the profitability of much of New York City's housing stock. Between April 1973 and mid-January 1974 the price of the two most common fuels, #4 and #6, rose 171% and 183% respectively. A survey in Washington Heights makes it clear that even sound, once-profitable middle-income buildings cannot sustain heating cost increases of this magnitude and continue to be operated as before.

1/ The Table 5 (p. 45) projected "Vacancy Decontrol increase" estimates by McKinsey appear to be gross overestimates of this source of income.

"In the ten buildings surveyed, (Table 1) monthly rentals average $38 per room, which is relatively high for the area. Fuel costs now consume 24% of gross income, as opposed to 9% at the end of last winter. In the three buildings with lowest rents (averaging $27 per room) the increase alone in fuel costs was equal to almost one quarter of the total rent roll. This points to severe operating problems for the City's marginal apartment buildings.

"Net cash flow has been cut by an average of 95%. Even more disturbing is the fact that only four of the ten buildings remain profitable to any significant extent; four previously profitable buildings are now losing money. If income from stores is excluded from consideration, only one of the ten buildings is making money from residential rents.

"It is difficult to exaggerate the seriousness of the problem which will result if the city does not take appropriate action. In the short run we can expect to see a sharp increase in the number of abandoned structures. In the long-run it is clear that essential maintenance will be cut, leading to an inexorable erosion in the quality of New York's moderate- and middle-income housing stock."

In order to generalize the foregoing observations, we may conservatively assume that aggregate fuel costs for this past winter have doubled. We know from the Sternlieb report that fuel costs in 1967 constituted from 4.8 to 19.4 percent of the total rent bill, averaging 10.2 percent (Table 2). Consequently, it may be estimated that this cost alone has impacted rents by ten percent.

Increases in labor costs will impact rents by another 2 percent. An estimated 10 percent increase in real estate taxes this year will add another 2 percent increase in rents. Mortgage refinancing annually adds about 1.5 percent to aggregate rent costs. The combined impact of the foregoing 1973-74 increases require a 15.5 percent increase in average rents for all families in order to leave owners no better off than they were in 1973.

The annual MBR increases will provide 7-1/2 percent for the remaining units under rent control (about 70-80 percent of the total normally under the MBR system). This aggregates to an average increase of 5-1/4 to 6 percent, which reduces to 4-1/2 to 5 percent because of buildings that are ineligible for these increases. About 2 percent will be recaptured from rent increases for the pass-along of increased labor costs. An additional increase of 3 percent in aggregate rents may be expected from increased income arising from decontrolled apartments. The foregoing increases are 9.5-10 percent compared with increased expenses of 15.5 percent which leaves a deficit of 5.5 to 6 percent of total rent rolls for owners in 1974. Thus the 1973 rent gap of $362 million between controlled rents and market rents estimated in my rent report will have increased by an additional $112 to $122 million as a result of the extraordinary cost increases of 1973-74 relative to the estimated increases in total rents in 1974.

Table 1.--EFFECTS OF HEATING COST INCREASES ON APARTMENT HOUSE OPERATIONS

	Net cash flow @ 4/73 fuel prices	Net cash flow @ 1/74 fuel prices	Monthly room rent*	New rent necessary to compensate for higher fuel prices	Store rentals as percentage of gross income
(1)	$18,443	$ 6,474	$43.30	$49 (+13%)	37%
(2)	13,541	(1,242)	42.11	48 (+14%)	
(3)	13,974	(1,348)	40.00	46 (+15%)	
(4)	8,363	(1,104)	24.02	30 (+23%)	
(5)	(3,645)	(14,281)	30.48	37 (+22%)	16%
(6)	2,282	(7,185)	25.60	31 (+22%)	
(7)	22,623	9,023	38.32	44 (+16%)	15%
(8)	25,048	11,518	37.67	43 (+15%)	
(9)	15,399	77	38.62	44 (+14%)	
(10)	14,863	3,842	48.41	55 (+13%)	20%
	$130,891	$5,865	$37.71	$44 (+15.7%)	9%

*Includes stores

Note: The above data make no corrections for differential consumption of fuel oil. To the extent that fuel consumption has been reduced from the previous heating period, the financial impact will be ameliorated.

Table 2.--COMPOSITE ESTIMATE OF FUEL AS A PERCENT OF NET RENTS RECEIVED FOR ALL RENT CONTROLLED BUILDINGS IN NEW YORK CITY, 1967

		Number of units (1968)	Fuel as a percent of net rents received
All units:		1,060,463	10.2
Type	Units		
Old law:	5-19	130,760	17.3
	20+	67,705	7.9
New law:	5-19	135,784	16.0
	20-49	329,597	9.9
	50+	180,662	6.5
Post 1929:	10-49	33,743	5.9
	50+	109,960	4.8
Small structures:	3&4	72,252	19.4

Source: George Sternlieb, The Urban Housing Dilemma, City of New York, Housing and Development Administration, 1972, Exhibit 1-1, p. 8, Exhibits 7-22 through 7-29, pp. 265-272.

Note that the foregoing assumes no action whatever with respect to vacancy decontrol. If vacancy decontrol were to be repealed effective July 1, the rent gap would be correspondingly increased by an additional $30 million to an estimated total of $504-$514 million--about the position ownerswere at in 1971. Aside from the devastating financial impact, the psychological impact will seriously diminish the willingness of owners to continue to maintain and operate their buildings under these adverse circumstances. We may confidently expect in 1974 that the rate of housing abandonment will increase from a level of approximately 10,000-12,000 in 1973 to a figure approaching the 20,000 level of 1969-70.

The McKinsey report is seriously deficient in its calculations of the financial effects of the past year's events to say nothing of the psychological effects of the proposal to repeal vacancy decontrol. Furthermore the McKinsey estimates (p. 60) of the rate of which decontrol will occur over time is grossly overstated--showing an accelerated rather than a decelerated rate of decontrol over time (see Table 3) with the result that the financial effects of decontrol over time are exaggerated (p. 65). It is not possible to rationalize the McKinsey estimates about the disappearing rent gap on p. 45. When the serious overstatements about the disappearance of the rent gap are taken into account, the McKinsey estimates of the costs of publicly supporting MBR deficits (p. 65) lose all validity.

The end result is that the McKinsey proposals violate both of its earlier cited objectives: maintenance of the existing housing inventory and maintaining balance between the financial needs of owners and tenants.

One final note. If we examine the wide variance in existing rents for the same space shown in Table 1 of my first memorandum to Mr. Bales, it becomes evident that the limitations of choice in the decontrolled market is not as narrow and does not limit renter options to nearly the degree that is assumed by the McKinsey report. The expressed concern about the adverse effects of decontrolled rents and increased rent-income ratios which result from moves from controlled to uncontrolled apartments is not supported by the evidence. We may note that families presently living in rent-controlled quarters who voluntarily propose to move, do so only after weighing the advantages of the new apartment and its location against the higher rent they presumably must assume as a result of their move. Newly formed households are at a disadvantage when they come into the uncontrolled market. But so have been all newly formed families in the past who were unable to find rent-controlled apartments and were forced to find housing in the uncontrolled part of the market. Certainly both the market and the range of choice is much larger for these families today.

Finally, it would not be at excessive public costs, as indicated in my memorandum to Carter Bales, to assist marginal-income families (not technically eligible for welfare assistance) to assume the higher rent costs created by decontrolled rents.

ATT.

Table 3.--ESTIMATE OF RATE OF DECONTROL OF THE RENT-CONTROLLED INVENTORY OVER TIME ASSUMING A 13 PERCENT RATE OF VACANCY TURNOVER

	Under control			Decontrolled
July 1, 1971	1,265,000	x $\frac{13\%}{2}$	=	82,000 during 1971
Dec. 31, 1971	1,183,000	x 13.0%	=	154,000 during 1972
Dec. 31, 1972	1,029,000	x 13.0%	=	134,000 during 1973
Dec. 31, 1973	895,000	x 13.0%	=	116,000 during 1974
Dec. 31, 1974	779,000	x 13.0%	=	101,000 during 1975
Dec. 31, 1975	678,000	x 13.0%	=	88,000 during 1976
Dec. 31, 1976	590,000			675,000

Note: The above method of calculation showing 895,000 controlled units (370,000 decontrolled) basically approaches the McKinsey calculation of 901,000 controlled units in 1973 (shown in Exhibit XXIV, p. 60) by using a 13 percent rate of turnover. But from 1974 onward, the McKinsey figures show an unexplainably accelerated rate of decontrol for which no known rationale exists.

THE McKINSEY REPORT
(Proposed by Carter F. Bales and Anupam Puri)

A CRITIQUE

by Robert S. Fougner

Preliminary Statement

The report reflects the familiar practice of using majestic rhetoric to reach a predetermined result by the issuance of "factual statements" without support in record facts or logic.

THE PREDETERMINED RESULT

It is decided a Proper Rent Control Program shall consist of:

1. Establishment of a buildingwide MBR, but without allocation to individual apartments.

2. Provide increases in collectible rents annually on a single percentage reflective of the average increase in "family income" for the City.

3. The Rent Gap between the building MBR and the allowable collections is to be subsidized by the City in the form of Tax Abatement.

THE PROBLEM

In order to make the facts fit the predetermined solution, namely, the subsidization of the rent gap by the City of New York, that gap must be shrunk sufficiently to avoid a claim of irresponsible action which would erode the tax base.

The Shrinking of the Rent Gap is Accomplished in two Opposing Procedures:

A. The increase in earnings since 1970 is overstated; and

B. The amount established as the fair return standard (i.e., 8½% of equalized assessed value) is reduced by $130 million.

A. The Overstatement of Post 1970 earnings by:

(1) Inaccurate recording of rent increases, and

(2) Incorrect consideration of increased expenses.

(1) The Increase in Income:

On pages 36-40, it is alleged that the original Rent Gap in 1970 was $805 million, but that (p. 40) this has allegedly been reduced by 73%. The only source for any of the authoritarian pronouncements is the January 1974 HDA Report also used as the basis for the Stein Report. The 73% reduction in the Rent Gap ($586 million) is accounted for as follows:

(a) 1970-1971 Local Law 30 interim increase	$ 85 million
(b) 1972 and 1973 MBR increase	150 "
Total controlled increase	$235 million

COMMENT: The foregoing presupposes that all apartments received complete collection of MBRs, but HDA claims nearly 300,000 units were denied.

(c) Vacancy decontrol increase	$351 million

COMMENT: The HDA survey does not support this calculation because:

(a) The variance between MBR and vacancy decontrol was found by HDA to be 16.2%. Since the Report ascribes 1/3 of the inventory to decontrolled apartments and 2/3 to controlled apartments, how can 1/3 of the stock rise by $351 million, with 2/3 (i.e., controlled) rising $235 million and yet the variance be only 16.2%? Since the Report uses the HDA statistics, it has misread or misunderstood the "facts" to achieve the predetermined result.

(b) The HDA survey flatly finds that the actual income of the properties (including vacancy decontrolled rents, but reflecting the depressed controlled rents artifically held below MBR by the 7½% limitation) is $300 million below MBR, yet the Report claims a variance of only 10% (p. 41).

(c) The Report claims the total of average decontrolled rent increases above prior controlled rents to be 78% (p. 36), yet the HDA survey on which it relies determined a figure of 52% and this was accepted by Stein. This is a 50% inflation of the HDA-Stein figure.

(d) The percentage figure of rent increases for controlled rents--34% since 1970--is suspect. The law provided for a maximum increase of 15% in the two years ending December 31, 1971 plus 7½% each in 1972 and 1973. This is a maximum of 32½% Even with variations for the $10 and $15 increases effective August 1, 1970 and the handful of 15% vacancy increases before 6/30/71, the Report presupposes a maximum increase for each unit. Thisignores the fact that HDA claimed more than 250,000 units received denials for lack of certification and about 80,000 December 31, 1971 rents were at or above MBR and received no MBR increase.

Understatement of Expenses

1. Fuel is calculated at increasing by "60% since 1972" (p. 43).

COMMENT: It is a fact that fuel remained fairly stable from 1971 to October 1973 at about 12¢ per gallon. The State in adopting its fuel pass-through regulation recognized a 100% increase between September and December 1973 from 12¢ to 22¢. The cost per gallon is now between 36¢ and 40¢. This is a trebling of the cost, far more than 60%. It is also stated that fuel is about 8% of rent, thus requiring a 5% pass-along of about $100 million. The Sternlieb Report indicates that fuel varied between 8 and 15% of rent in 1967-70. As the result of the Arab blockade, it now runs from 20 to 40%. In addition, the cost of electricity has soared. The Report alleges that part of the fuel increase since 1972 is reflected in the 1974 MBR calculation. The fact is that the HDA Report of January 1974 on which McKinsey relies acknowledges that its operating studies for the 1974 MBR did not go beyond June 30, 1973. Hence, no part of the fuel increase is reflected in the new

MBR.

2. Based on the McKinsey Report (p. 45), the January 1, 1974 Rent Gap is $219 million; the HDA Report places it at above $300 million. The McKinsey Report projects increases and decreases in this Rent Gap as follows (p. 45):

January 1974	$219 million
1974 MBR Revision	174 "
Fuel Increase	100 "
Total	$493 million

Answer:

January 1974 Gap as per HDA	$300 million
1974 MBR when issued	174 "
Added fuel cost	300 "
Total	$774 million

McKinsey Reduction in Rent Gap

1974 MBR Collectible rent increase	$ 80 million
Vacancy decontrol to 1975	210 "
Fuel Passthrough	100 "
Total	$390 million

Answer:

The 1974 MBRs are running behind. The $80 million will not be received on time.

Vacancy decontrol is targeted for discontinuance and the fuel pass-through has been rejected. For the present, this leaves the gap at $774 million. Even if vacancy decontrol is not terminated, it cannot account for $219 million because it only exceeds MBR by 16% and affects one-third of the housing at a maximum.

3. The Modification of MBR Return

The Report contends that the owners are being "overcompensated" (p. 46). Thus to remove the Rent Gap, the return is reduced by $130 million.

COMMENT: Since the first two years of MBR reflected $150 million of increased income, this $130 million cut would reduce about 20 months of MBR increasea and produce a catastrophe.

Other Defects

1. The establishment of a building MBR without apartment allocation will return one of the evils MBR was allegedly designed to terminate, namely "rent skewing".

2. The limitation of annual adjustments to a so-called average family income increase is fallacious. What happens if there is a reduction? Should rents then be reduced?

3. No provision is made for hardship earnings situations where the MBR itself does not reflect a fair return on the individual expenses of the property.

4. In view of the obvious understatement of the Rent Gap, it is clear that instead of a $50 million subsidy the City would have to contribute, the figure is closer to $500 million.

CONCLUSION

The report is based on misconceptions of statistics without any real understanding of the operation of the rent control program, the true measure of increased expenses and the HDA's own figures as to changes in rents. The artificial reduction in the rent gap to induce the City to subsidize the difference is transparent and unrealistic. The only way to bridge the rent gap is by a threefold contribution including Government, tenants and owners. Neither Government alone, owners alone or tenants alone should be asked to shoulder the burden.

The proposal to scuttle the existing MBR for another long-term change is simply not in the cards. The present MBR system can be made to work by avoiding complex calculations and simply building on the 1972 MBR by the application of standard BLS operating cost index figures.

// During 1950 to 1970, we estimate that less than 21 percent of the new housing built directly benefited low-income groups.

Conversions. The rate of additions to the housing stock through conversions declined from the 1950s to the 1960s. This is likely to be a negligible source of new housing units in the future.

Demolitions. Demolitions occur primarily as a function of planned redevelopment of neighborhoods, inside or outside urban renewal areas. In addition, buildings are demolished by the City when they become health or safety hazards. Viewed over the past two decades, the number of demolitions has been relatively constant.

Abandonments. Abandonments of housing have become as important a factor in reducing the active housing inventory as demolitions, and are now embedded in the national consciousness as a unique and disturbing feature of the central city housing crisis. Three features of the abandonment problem are especially important:

- The rate of abandonment has climbed dramatically. During the 1950s, no recorded abandonment occurred. During the 1960s, about 10,000 units were abandoned annually. Moreover, this rate climbed from 4,000 to 6,000 units annually in the period 1960 to 1964 to an estimated annual rate of 18,000 to 20,000 abandonments at the end of the 1960s.

- Most of these abandoned buildings are still standing. Frank Kristof of the Urban Development Corporation has estimated that about 75 percent of the buildings abandoned in New York City are still standing. These buildings become major hazards to health and safety, encourage vandalism and crime, and can quickly blight an area with serious adverse effects on surrounding neighborhoods.

- Much of the housing abandoned in the City was structurally sound. While little is known about the details of abandoned buildings (because the abandonment is often not recorded until much later, by which time the building has been vacated and often vandalized beyond recognition), a disturbing phenomenon is that many of the abandoned buildings appear to be structurally sound. For example, the Citizens Budget Commission has estimated that 60 percent of the abandoned buildings could, with minor rehabilitation, have continued to provide decent housing to their occupants. Loss of

structurally sound housing through abandonment has come to be recognized as one of New York City's central housing problems.

Why do these abandonments occur? The basic reasons are by now well known: They include a process of neighborhood erosion caused by ethnic turnover, declining income, declining rents, and a significant reduction in landlords' ability to maintain their properties.

The overall stability of New York City's population masks a dramatic change in ethnic composition and income levels. Between 1950 and 1960, the proportion of nonwhites rose from 10 to 14 percent of the City's population; by 1970, this figure had increased to 21 percent. In addition, the newcomers were increasingly low-income families - between 1950 and 1960, the percentage of families earning less than $4,000 declined from 31.2 to 18.1 percent; by 1970, the percentage of families under $4,000 had grown to 32.9 percent. And this trend occurred despite a growth in the number of Social Security beneficiaries to over 1 million, with another 1.3 million persons on welfare.

Given the low incomes of the new residents, previous rent levels in the City could not be sustained. Lower incomes, a relative concentration of the newcomers in limited areas of the City - with the existing neighborhood population fleeing, in part, due to racial prejudice - led to a process in which landlords significantly shortened their investment horizons, found their properties increasingly unsalable, decided to underinvest in maintaining those properties, and ultimately decided that it was more desirable to abandon their properties than to attempt to maintain them.

The process of abandonment had disastrous effects on housing in New York City. Not only were entire neighborhoods doomed, but the total stock of housing began to shrink (Exhibit VI). It became increasingly obvious that the prime focus of housing policy had to be to reduce the rate of abandonment and to ensure that the City's existing housing stock was preserved, rather than to raise the production rate of new housing.

SERVICES FROM THE HOUSING STOCK

The significant shift in the factors affecting the size of the housing stock during the late 1960s was much less important than the change in the quality of the existing housing stock, and in the nature of housing services afforded to its occupants.

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Corporation Counsel is then requested by the Director of Demolition to obtain a court order for demolition. A hearing is set by a judge and, in due course, a precept or final order is issued. The Department then lets contracts for the demolition and places a lien against the property to recoup the cost. Legally, the property remains in the hands of the owner who abandoned it, encumbered by the lien, but providing no rental income.

It normally takes between six months and a year to initiate and complete the demolition process although, in emergencies, the time can be shortened to a few months. It is estimated that about 53 percent of the buildings that enter the pipeline are eventually torn down.

In 1965, a total of 265 buildings was razed by the City by this process. In 1966, the figure rose to 418. Beginning in 1967, the program was substantially expanded to extend to 1,000 buildings in 1967, 1,375 in in 1968 and 1,500 in 1969. In addition, 450 buildings were torn down by owners in 1969. No precise figure exists on the number of rental units in the demolished structures. A recent study by HDA put the average at 3 units per building, but non-government sources estimate the figure to be higher.

It is difficult to determine how many of the demolished buildings could have been renovated, but it has been roughly estimated that between 50 and 60 percent of them were structurally capable of being renovated. It is estimated that about 30 percent of demolished buildings were old-law tenements which are not usually structurally susceptible of renovation. The rest were not structurally suitable for renovation for other reasons. It is however much more difficult to obtain valid estimates as to the percentage of demolished buildings the renovation of which would be economically feasible.

Renovation of Vacant Buildings

The Municipal Loan Program is the source of financing for most vacant building renovation work. This program was established in 1961 by executive order

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It is difficult to determine how many of the demolished buildings could have been renovated, but it has been roughly estimated that between 50 and 60 percent of them were structurally capable of being renovated. It is estimated that about 30 percent of demolished buildings were old-law tenements which are not usually structurally susceptible of renovation. The rest were not structurally suitable for renovation for other reasons. It is however much more difficult to obtain valid estimates as to the percentage of demolished buildings the renovation of which would be economically feasible.

Renovation of Vacant Buildings

The Municipal Loan Program is the source of financing for most vacant building renovation work. This program was established in 1961 by executive order

Corporation Counsel is then requested by the Director of Demolition to obtain a court order for demolition. A hearing is set by a judge and, in due course, a precept or final order is issued. The Department then lets contracts for the demolition and places a lien against the property to recoup the cost. Legally, the property remains in the hands of the owner who abandoned it, encumbered by the lien, but providing no rental income.

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// During 1950 to 1970, we estimate that less than 21 percent of the new housing built directly benefited low-income groups.

Conversions. The rate of additions to the housing stock through conversions declined from the 1950s to the 1960s. This is likely to be a negligible source of new housing units in the future.

Demolitions. Demolitions occur primarily as a function of planned redevelopment of neighborhoods, inside or outside urban renewal areas. In addition, buildings are demolished by the City when they become health or safety hazards. Viewed over the past two decades, the number of demolitions has been relatively constant.

Abandonments. Abandonments of housing have become as important a factor in reducing the active housing inventory as demolitions, and are now embedded in the national consciousness as a unique and disturbing feature of the central city housing crisis. Three features of the abandonment problem are especially important:

- The rate of abandonment has climbed dramatically. During the 1950s, no recorded abandonment occurred. During the 1960s, about 10,000 units were abandoned annually. Moreover, this rate climbed from 4,000 to 6,000 units annually in the period 1960 to 1964 to an estimated annual rate of 18,000 to 20,000 abandonments at the end of the 1960s.

- Most of these abandoned buildings are still standing. Frank Kristof of the Urban Development Corporation has estimated that about 75 percent of the buildings abandoned in New York City are still standing. These buildings become major hazards to health and safety, encourage vandalism and crime, and can quickly blight an area with serious adverse effects on surrounding neighborhoods.

- Much of the housing abandoned in the City was structurally sound. While little is known about the details of abandoned buildings (because the abandonment is often not recorded until much later, by which time the building has been vacated and often vandalized beyond recognition), a disturbing phenomenon is that many of the abandoned buildings appear to be structurally sound. For example, the Citizens Budget Commission has estimated that 60 percent of the abandoned buildings could, with minor rehabilitation, have continued to provide decent housing to their occupants. Loss of

under Article 8 of the Private Housing Finance Law and is administered by the Office of Rehabilitation Financing in the Department of Development of the Housing and Development Administration. It offers 90 percent loans to private developers seeking to renovate buildings. The loans are generally at 5½ percent interest for a period of 30 years. They pay up to 90 percent of the following costs:

cost of construction
payment and performance premium
relocation
architects' fees
existing mortgages
interim interest
interim taxes
title and recording
mortgage recording tax.

From its inception in 1961 to November 30, 1969 the program has made loans totalling. $56,549,229 for the renovation of 5,214 units in 334 buildings throughout the City. The program got off to a slow start and has gradually gathered momentum. Most of the loans have been closed recently. For example, in the first 11 months of 1969, 1,339 units in 73 buildings were renovated, representing more than 25 percent of the units and 20 percent of the structures.

The loans generally total from $10,000 to $14,000 per unit being renovated. Apartments, once renovated under this loan program, rent for an average of $33 a room a month. About half of the renovated buildings were initially abandoned and about 80 percent are in model cities, urban renewal, or code enforcement areas. Recently the program has experimented with renovation of contiguous buildings which now constitute 5 percent of the renovation output. The Office of Rehabilitation Financing maintains a staff of 40 technical employees (construction inspectors, rehabilitation specialists, plumbers, electricians and engineers) who examine preliminary plans and final drawings, and supervise construction work. The director of the program estimates that the total figures for 1969 will equal the total output for the seven previous years.

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